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PENNSYLVANIA BUSINESS LAW.

A PRACTICAL HANDBOOK FOR BUSINESS
MEN AND LAWYERS.

BY

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THIS VOLUME IS RESPECTFULLY
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TABLE OF CONTENTS.

INTRODUCTION.....	PAGE 15
-------------------	------------

BOOK FIRST—CONTRACTS IN GENERAL.

PART I.

THE FORMATION OF CONTRACTS.

CHAPTER I.—THE DIVISIONS OF CONTRACT LAW AND THE DEFINITION OF A CONTRACT	17
CHAPTER II.—THE FIRST ELEMENT NECESSARY IN ALL CONTRACTS, OFFER AND ACCEPTANCE	23
CHAPTER III.—THE SECOND ELEMENT NECESSARY IN ALL CONTRACTS, SEAL OR CONSIDERATION	56
(A) Seal.	57
(B) Consideration	60
CHAPTER IV.—THE THIRD ELEMENT NECESSARY IN ALL CONTRACTS, CAPACITY OF PARTIES	84
(A) Contractual powers of minors	87
(B) Contractual powers of persons mentally deficient. ...	95
(C) Contractual powers of married women	97
(D) Contractual powers of corporations.	99
(E) Contractual powers of foreigners.	100
CHAPTER V.—THE FOURTH ELEMENT NECESSARY IN ALL CONTRACTS, REALITY OF CONSENT	101
(A) Mistake	102
(B) Misrepresentation	104
(C) Fraud	106
(D) Undue influence	110
(E) Force	112
CHAPTER VI.—THE FIFTH ELEMENT NECESSARY IN ALL CONTRACTS, LEGALITY OF OBJECT	114
(A) Agreements violating constitutional or statute law or federal treaties	115
(B) Agreements interfering with the public government. ...	119
(C) Agreements injurious to the people at large or to particular individuals	120

	PAGE
CHAPTER VII.—THE SIXTH ELEMENT NECESSARY IN A FEW CONTRACTS, SPECIAL FORMALITY	123
(A) Sales of real estate, and certain other realty contracts	123
(B) Trusts as to real estate	125
(C) Contracts reducing an absolute conveyance to a mortgage	127
(D) Contracts of suretyship and guaranty	129
(E) Contracts of apprenticeship	131

PART II.

THE OPERATION OF CONTRACTS.

CHAPTER VIII.—A CONTRACT WHEN FORMED USUALLY OPERATES ONLY ON THOSE WHO ARE PARTIES TO IT.	133
CHAPTER IX.—AFTER THE FORMATION OF A CONTRACT, RIGHTS AND OBLIGATIONS CREATED BY IT MAY SOMETIMES BE PASSED TO OUTSIDERS BY SUBSEQUENT AGREEMENT OR BY OPERATION OF LAW	134
(A) Assignment by subsequent agreement	134
(B) Assignment by operation of law	137
CHAPTER X.—NEGOTIABLE CONTRACTS	138
(A) Negotiable instruments act of May 16, 1901	144
(B) Other acts concerning negotiable instruments for the payment of money	179
(C) An act concerning bills of lading and warehouse receipts	180

PART III.

THE INTERPRETATION OF CONTRACTS.

CHAPTER XI.—RULES OF EVIDENCE RELATING TO CONTRACTS	181
CHAPTER XII.—RULES FOR THE CONSTRUCTION OF CONTRACTS	183

PART IV.

THE DISCHARGE OF CONTRACTS.

CHAPTER XIII.—DISCHARGE OF CONTRACTS BY AGREEMENT	185
(A) By contract of release	185
(B) By contract of novation	186
(C) By the operation of a condition subsequent in the original contract itself	186

Contents.

7

	PAGE
CHAPTER XIV.—DISCHARGE OF CONTRACTS BY PERFORMANCE	187
CHAPTER XV.—DISCHARGE OF CONTRACTS BY BREACH	189
CHAPTER XVI.—DISCHARGE OF CONTRACTS BY IMPOSSIBILITY	195
CHAPTER XVII.—DISCHARGE OF CONTRACTS BY BANKRUPTCY	196
(A) The United States Bankruptcy Act	198
(B) Forms of accounts in bankruptcy procedure	242
(C) The Pennsylvania Insolvency Act of June 4, 1901.	246

BOOK SECOND—AGENCY, PARTNERSHIPS AND CORPORATIONS.

PART I.

AGENCY.

CHAPTER XVIII.—THE FORMATION OF AGENCY	273
(A) Agency created by express agreement	274
(B) Agency created by appointment	275
(C) Agency created by estoppel	275
(D) Agency created by ratification	276
CHAPTER XIX.—THE TERMINATION OF AGENCY	277
(A) Termination of agency by agreement	278
(B) Termination of agency by performance	279
(C) Termination of agency by breach	279
(D) Termination of agency by impossibility	280
(E) Termination of agency by bankruptcy	281
CHAPTER XX.—THE RIGHTS AND OBLIGATIONS OF PRINCIPALS, AGENTS AND THIRD PARTIES	281
(A) The agent's obligations towards his principal	282
(B) The agent's obligations towards third parties	284
(C) The principal's obligations towards his agent	285
(D) The principal's obligations towards third parties	288
(E) The obligations of third parties towards the principal.	290
(F) The obligations of third parties towards the agent.	291

PART II.

PARTNERSHIPS.

	PAGE
CHAPTER XXI.—THE FORMATION OF PARTNERSHIPS	292
CHAPTER XXII.—THE TERMINATION OF PARTNERSHIPS.....	302
(A) Termination of partnerships by agreement	302
(B) Termination of partnerships by performance	305
(C) Termination of partnerships by breach.....	305
(D) Termination of partnerships by impossibility	306
(E) Termination of partnerships by bankruptcy or insol- vency	308
CHAPTER XXIII.—THE RIGHTS AND OBLIGATIONS OF PARTNERS....	309
(A) The relation of a partner towards his fellows as a co-proprietor of the firm	309
(B) A partner's authority as an agent of the firm.....	311
(C) A partner's obligations towards firm creditors.....	318
(D) Partnership accounts	320
CHAPTER XXIV.—PARTNERSHIPS FORMED UNDER PENNSYLVANIA STATUTES	324
(A) Special partners under the act of March 21, 1836....	325
(B) Limited partnership associations under the act of June 2, 1874.....	334
(C) Limited partnership associations under the act of May 9, 1899.....	341
(D) Bonus on capital	347

PART III.

CORPORATIONS.

CHAPTER XXV.—THE FORMATION OF CORPORATIONS	349
(A) Formation of corporations of the first class	353
(B) Formation of corporations of the second class	354
CHAPTER XXVI.—THE TERMINATION OF CORPORATIONS.....	360
(A) Termination of corporations by agreement	360
(B) Termination of corporations by performance	362
(C) Termination of corporations by breach	363
(D) Termination of corporations by impossibility.....	364
(E) Termination of corporations by insolvency or bank- ruptcy.....	364

	PAGE
CHAPTER XXVII.—ADMISSION TO MEMBERSHIP IN A CORPORATION, EXPULSION THEREFROM AND TRANSFER OF INTERESTS THEREIN	372
(A) Membership in corporations of the first class.....	372
(B) Membership in corporations of the second class.....	373
(C) Powers of attorney to transfer stock.....	377
(D) Fraudulent issue of stock by corporate officers.....	380
(E) Practical rules about stock certificates for the guidance of stockholders	382
CHAPTER XXVIII.—THE RIGHT OF STOCKHOLDERS AND OTHER MEM- BERS OF CORPORATIONS TO A SHARE OF PROFITS.....	385
(A) A stockholder's right to dividends.....	385
(B) The rights of preferred stockholders	387
(C) The right to a dividend as between various claimants	388
(D) A stockholder's right to subscribe for new stock ...	390
CHAPTER XXIX.—THE RIGHTS OF STOCKHOLDERS AND OTHER MEM- BERS OF CORPORATIONS TO CONTROL AND INSPECT CORPORATE AFFAIRS	390
(A) The right of a member to vote at the election of corporate directors	392
(B) The manner of conducting meetings of corporate members	394
(C) The business transacted at meetings of corporate members.....	396
(D) The right of a member to inspect corporate books.	400
CHAPTER XXX.—THE LIABILITIES OF STOCKHOLDERS AND OTHER MEMBERS OF CORPORATIONS	401
(A) Liability on stock subscriptions	402
(B) Release of a stockholder's liability by subsequent agreement with the corporation.....	406
(C) Liability of original subscribers and other stock- holders to pay assessments.....	407
(D) Liability of stockholders for certain corporate debts.	410
CHAPTER XXXI.—THE RIGHTS AND OBLIGATIONS OF CORPORATE DIRECTORS	411
(A) The rights and powers of directors.....	411
(B) The obligations and liabilities of directors.....	415
CHAPTER XXXII.—THE RIGHTS AND OBLIGATIONS OF THE PRESI- DENT AND OTHER CORPORATE OFFICERS.....	420
(A) The President	420
(B) The Secretary	422
(C) The Treasurer.....	422

	PAGE
CHAPTER XXXIII.—THE MERGER AND CONSOLIDATION OF CORPORATIONS	423
(A) Corporations of the first class.....	423
(B) Corporations of the second class	424

CHAPTER XXXIV.—PENNSYLVANIA BONUS AND TAX LAWS; REGULATION OF DOMESTIC AND FOREIGN COMPANIES	429
(A) Bonus and taxes.....	430
(B) Reports and registration.....	432
(C) Domestication of foreign corporations.....	436

BOOK THIRD—PERSONAL AND REAL PROPERTY.

PART I.

BAILMENTS, INCLUDING CONTRACTS FOR PLEDGING, HIRING AND TRANSPORTING PERSONAL PROPERTY.

CHAPTER XXXV.—THE DEFINITION OF A BAILMENT AND VARIOUS FORMS THEREOF.....	439
CHAPTER XXXVI.—THE BAILEE'S DUTIES AND OBLIGATIONS.....	442
(A) Towards the bailor.....	442
(B) Towards third parties.....	447
CHAPTER XXXVII.—THE BAILOR'S DUTIES AND OBLIGATIONS	448
(A) Towards the bailee.....	448
(B) Towards third parties	455
CHAPTER XXXVIII.—DUTIES AND OBLIGATIONS OF THIRD PARTIES	457
(A) Towards the bailor	457
(B) Towards the bailee	458
CHAPTER XXXIX.—TRANSPORTATION OF PERSONAL PROPERTY.....	462
(A) Who is a common carrier of goods	462
(B) Duty to receive and carry	464
(C) Delivery to carrier ..	464
(D) Bills of lading	466
(E) Duty to carry safely and to furnish facilities; discrimination	468

Contents.

II

	PAGE
(F) Custody and control of goods, and rights in them	470
(G) Termination of liability; delivery by carrier.....	471
(H) Baggage	472

PART II.

SALES OF PERSONAL PROPERTY.

CHAPTER XL.—THE DEFINITION OF A SALE, AND DISTINCTIONS BETWEEN SALES AND BAILMENTS.....	476
CHAPTER XLI.—THE TRANSFER OF TITLE FROM SELLER TO PURCHASER	486
(A) When the title passes to the buyer	486
(B) What title passes to the buyer.....	488
CHAPTER XLII.—THE RIGHTS OF THE SELLER OF PERSONAL PROPERTY	495
(A) The seller's right to set the contract aside on the ground of fraud.....	495
(B) The seller's lien for the purchase money	498
(C) The seller's right of stoppage in transit.....	499
CHAPTER XLIII.—THE RIGHTS OF THE PURCHASER OF PERSONAL PROPERTY	501
(A) The purchaser's right to demand goods of a certain quality	501
(B) Warranty of the purchaser's title.....	508

PART III.

LEASES OF REAL PROPERTY.

CHAPTER XLIV.—THE FORMATION OF THE RELATION OF LANDLORD AND TENANT.....	510
(A) Contracts of lease implied from the conduct of the parties	510
(B) Leases by word of mouth	512
(C) Written or printed leases.....	513
CHAPTER XLV.—THE LANDLORD'S RIGHTS	521
CHAPTER XLVI.—THE TENANT'S RIGHTS.....	527

PART IV.

SALES OF REAL PROPERTY.

	PAGE
CHAPTER XLVII.—CONTRACTS TO SELL REALTY AND CONVEYANCES	
THEREOF	534
(A) The formation of a contract to sell realty.....	534
(B) The performance of a contract to sell realty by delivery of the deed	540
(C) The necessity of recording	546
CHAPTER XLVIII.—RIGHTS AND OBLIGATIONS OF THE PARTIES TO A SALE OF REAL ESTATE AFTER THE TITLE HAS PASSED.....	550
(A) The obligations of the seller towards the purchaser	550
(B) The obligations of the purchaser towards the seller.	556

BOOK FOURTH—SURETYSHIP AND GUARANTY,
AND INSURANCE.

PART I.

SURETYSHIP AND GUARANTY.

CHAPTER XLIX.—THE NATURE AND FORMATION OF THE CONTRACT.	559
(A) Nature of the contract	559
(B) Formation of the contract	561
1. Formality and consideration.....	561
2. Parties; agency; partnership; co-sureties....	562
3. Communication of acceptance.....	564
4. Reality of consent.....	565
CHAPTER L.—THE TERMINATION OF THE CONTRACT.....	567
(A) Discharge by agreement	567
(B) Discharge by performance	568
(C) Discharge by breach	568
(D) Discharge by impossibility.....	570
(E) Discharge by bankruptcy.....	571
CHAPTER LI.—RIGHTS AND OBLIGATIONS OF THE PARTIES	571
(A) Obligations of creditor towards surety or grantor...	571
1. To take action against the principal	571
2. To give notice of the principal's default....	574
(B) Obligations of surety or guarantor towards creditor.	575
(C) Obligations of principal towards surety or guarantor.	577
CHAPTER LII.—FORM OF AGREEMENT	579

PART II.

INSURANCE.

	PAGE
CHAPTER LIII.—FIRE INSURANCE	582
(A) Who has an insurable interest.....	582
(B) Formation of the contract.....	586
(C) Reality of consent.....	589
(D) Conduct of insured after policy is issued.....	590
(E) What risks are covered.....	591
(F) Transfer of policies	592
(G) Notice and proofs of loss.....	594
(H) Rights of insurance company against incendiary and others.....	595
CHAPTER LIV.—FORM OF FIRE POLICY AND MORTGAGEE CLAUSE....	596
CHAPTER LV.—LIFE INSURANCE	602
(A) Who has an insurable interest.....	603
(B) Beneficiaries; payment of the first premium.....	604
(C) Reality of consent.....	606
(D) Suicide; execution for crime	607
(E) Statutory regulation of insurance companies and agents.....	607

BOOK FIFTH—THE ESTATES OF DECEDENTS.

PART I.

THE MANAGEMENT OF DECEDENTS' ESTATES.

CHAPTER LVI.—THE GRANTING OF AUTHORITY TO ADMINISTRA- TORS AND EXECUTORS AND THE REVOCATION THEREOF	609
CHAPTER LVII.—THE DUTIES OF EXECUTORS AND ADMINISTRATORS AFTER THEY HAVE QUALIFIED	622
(A) Inventory and appraisement.....	622
(B) Powers and duties of executors and administrators	625
(C) Payment of collateral inheritance and other taxes	637
(D) Advancements	640
(E) Widow's and children's exemption	642
CHAPTER LVIII.—THE ACCOUNTS OF EXECUTORS AND ADMINISTRA- TORS, AND THE FINAL STEPS IN CLOSING AN ESTATE.....	643
(A) Auditing the account	645
(B) Form of executor's or administrator's account	652
(C) The discharge, removal or death of an executor or administrator	658

PART II.

THE INTESTATE LAW, WILLS AND TRUST ESTATES.

	PAGE
CHAPTER LIX.—THE INTESTATE LAW	663
CHAPTER LX.—WILLS.....	673
(A) General statutory provisions.....	673
(B) Form of will.....	681
(C) Will contests	683
(D) Revocation of wills.....	684
CHAPTER LXI.—TRUST ESTATES	686
(A) Various kinds of trusts.....	686
(B) Rights, powers and duties of trustees.....	693
(C) Limits upon the duration of trust estates and upon the accumulation of income	696

INTRODUCTION

A practical book on Business Law must set forth not only the principles of the old Common Law which come to us from England, but also the numerous statutes and judicial decisions by which the Common Law has been altered to fit modern conditions. The statutes and decisions of different States vary widely, and it is perhaps impossible to give within the limits of a single volume the law of over forty States concerning the many legal subjects with which a business man should be acquainted. The present work is, therefore, devoted to a treatment of the law in Pennsylvania.

The Commonwealth of Pennsylvania is a distinct sovereignty, with its own constitution and its own executive, legislative and judicial branches of government. Except in so far as it has ceded a portion of its powers to the Federal Government at Washington, it is complete in itself and independent. The United States Judiciary has a certain power to set aside the decisions of our State courts and the acts of our Legislature when in conflict, as infrequently happens, with the United States Constitution, laws or treaties, but otherwise the Pennsylvania Legislature and Judiciary are secure from outside interference. The legal system which has been developed in Pennsylvania is worthy of every citizen's study. A knowledge of the law is no longer regarded as the property of lawyers alone. Everybody is bound at his peril to know it so far as it applies to himself and his affairs. Ignorance of it is no excuse.

Apart from the utility of this study, there is its great educational advantage. It is a science which combines the exactness of logic with such flexibility that it can be adapted to meet the ever changing needs of an American commonwealth. It has, furthermore, a human interest which appeals to everybody. In the following pages, the reader should try to get not merely

an understanding of legal rules, but also an appreciation of their justice, wisdom and harmony, for they are based upon the experience of many generations.

The five books into which this volume is divided are arranged in a natural order. The first book concerns contracts in general. This is the most important subject in Business Law. The second book begins by showing how contracts may be formed through agents who represent the parties in interest. The chapters on agency explain also the relations of agents and their employers towards each other and towards third parties. In the succeeding chapters on partnership we are introduced to a more complicated situation, for each member of a partnership is its agent and at the same time one of the proprietors. Then we consider certain kinds of limited partnerships which gradually approach in their legal features the character of a corporation. Book second concludes with a number of chapters about Pennsylvania corporations.

Book third deals with property rights and special contracts concerning property. Sales and leases of real estate are considered, as well as similar transactions affecting personal property. In the fourth book contracts of suretyship and guaranty and various kinds of insurance contracts are treated. In the fifth book the subject of decedents' estates is taken up, together with wills and the intestate law of Pennsylvania. A number of forms for the guidance of business men are introduced in appropriate places. Specimens of accounts used in bankruptcy, real estate and Orphans' Court matters are also included.

Paul C. Hamlin, Esq., of the Philadelphia bar, has rendered valuable assistance in the production of this work, especially of book fourth, concerning Suretyship and Guaranty, and Insurance. Mr. F. Markoe Rivinus has also rendered valuable assistance in preparing the volume for the press, and in verifying and discussing with the author its authorities.

JOHN J. SULLIVAN.

*Land Title Building, Philadelphia,
September 1, 1906.*

BOOK FIRST

CONTRACTS IN GENERAL

PART I

THE FORMATION OF CONTRACTS

CHAPTER I.

THE DIVISIONS OF CONTRACT LAW AND THE DEFINITION OF A CONTRACT.

In the first book of this work the general principles of contract law will be treated. Most of these principles apply in one and the same way to all kinds of contracts. In the succeeding books we shall take up, among other things, many special principles relating to particular classes of contracts. This first book, dealing with the general rules of contract law, is divided into four parts. The first part concerns the formation of a contract. The second part concerns the operation of the contract after it is formed. The third part concerns the interpretation of the contract if it needs to be explained and construed in legal proceedings. The fourth part concerns the discharge of the contract, that is to say, its termination.

In these four parts of the first book we follow a contract from the cradle to the grave. In the first place, we ask how it is made and what things are required to form a perfect contract. In the second place, we ask about the effect of the contract after it has been properly formed. Upon what persons

does it have any legal bearing? Who are benefited by it or put under any duty by it? Who gains any new right or incurs any new responsibility by reason of it? In the third place, we ask how the courts will interpret the contract. How shall its terms be proved? If the contract has been put in writing, how far can it be explained or varied by verbal testimony? What rules are applied by the courts in sifting out the meaning of the contract from a mass of tangled and contradictory terms? In the fourth place, we ask how the contract comes to an end. In what various ways may a person who has assumed liability under a contract unburden himself? How may the rights which are obtained through the contract be satisfied? How may it be finally squared up and settled forever?

Of the four main divisions just named, the first will require more study than the other three together. The first has to do with the making of a contract. If a contract is carefully made, it will in most cases run along until its final termination without causing lawsuits and without raising doubts as to whom it should affect, or how it should be interpreted or when it is fulfilled and discharged. Indeed, almost all the rules of contract law relating to the various stages in the existence of a contract after it has been formed are focused upon its original formation. The terms originally settled upon are of constant importance throughout the life of the agreement, no matter what emergency may arise; and by forming a contract with an eye to future legal contingencies one will gain advantages which may prove valuable afterwards. The business man is especially interested in the formation of a contract. Most contracts are made without securing professional advice, but if trouble arises subsequently resort to a lawyer is then had. You should, therefore, devote special attention to the first main division of contract law.

This first main division, relating to the formation of a contract, is subdivided into six parts: first, Offer and Acceptance; second, Seal or Consideration; third, Capacity of Parties; fourth, Reality of Consent; fifth, Legality of Object; sixth, Special Formality.

Each of these six subdivisions designates an element which is necessary as an ingredient in the making of valid and enforceable contracts. The first five elements are necessary in all contracts. The sixth element, Special Formality, is necessary in the formation of a few classes of contracts. The first element, Offer and Acceptance, means the agreement, the meeting of the minds of the contracting parties, which is obviously required to make a contract. The second element, Seal or Consideration, is harder to understand, and it will be carefully explained later. The third element, Capacity of Parties, is plainly necessary, because the parties to any agreement must be legally capable of entering into that agreement; otherwise it will not be valid. The fourth element, Reality of Consent, is necessary, for if the consent of both parties is founded upon a complete mistake as to an essential fact, the basis of the agreement is unsubstantial, and their consent is only superficial and apparent, not real; and, likewise, if one of the parties has been induced by the other to make the agreement on the faith of the other's fraudulent representations, or through the other's violence or improper influence, the consent of the victim of fraud or oppression is not genuine. The fifth element, Legality of Object, is necessary, because the law must not be used as a means to perpetrate wrong. If two men make an agreement to accomplish an illegal object, the courts will not enforce that agreement, for to do so would be to lend the instruments of justice to the promotion of injustice, which would be absurd. The sixth element, Special Formality, is necessary in a few kinds of contracts which will be considered hereafter. These six elements will be treated one by one in the six following chapters.

Let us see what a contract is. Anson defines it as "an agreement enforceable at law, made between two or more persons, by which rights are acquired by one or more to acts or forbearances on the part of the other or others." This definition should be closely examined.

The word "agreement" in the definition means an exact, complete meeting of the minds of the contracting parties. There must be nothing vague or hazy about it. There must

be no doubt or difference as to terms. The words "enforceable at law" mean that the agreement must be of such a character that, if it is broken, it will commend itself to the courts as proper and suitable to be upheld and enforced against the party who violates it. The ordinary business agreement is of this character, and is enforceable at law. A purely social agreement between two persons to dine together or to travel together is not enforceable at law, because no useful purpose would be served by enforcing such agreements, and the parties themselves, when they make social engagements, do not regard them as solemn undertakings which the law may be invoked to uphold. If two persons make plans to journey abroad for pleasure, and agree to go together merely to enjoy each other's company, their arrangement may be cancelled by one of them without giving the other any right to seek damages in an action at law. Under ordinary circumstances such an agreement is not meant to be legally binding on the parties, and the courts will not regard it as a contract, the breach of which entails legal responsibility. On the other hand, if a man who expects to go to Europe engages a courier, and subsequently changes his mind, the courier may sue him for damages, because the agreement between the two parties would be a purely business agreement.

In weighing the meaning of the words "enforceable at law," we may go back to the primitive days when no agreements were enforceable at law. When a community first becomes civilized and establishes a government, the officers of that government have enough to do in preserving order and keeping out foreign invaders. As the commerce of the community grows, history tells us that it becomes desirable for the government to take up the problem of promoting good faith and credit by forcing citizens to live up to certain agreements. When the government of an advancing community undertakes this additional function, it is usually content in the beginning to enforce only the most solemn engagements. As co-operation develops more and more, the need of making every member of the complex social organism abide by his agreements increases, and in a country like the United States it is

essential to the spread of commerce that the government shall lend its aid to make citizens live up to thousands of different kinds of business agreements. If an agreement is clearly outside of the sphere of state interference it is not enforceable at law. An instance of one sort of agreement with which the State should not concern itself is an agreement to become a member of this or that religious body. If one man agrees with another that they shall both join a new religious sect, the parties will not be making a *contract*, because their agreement will not be of the kind which the courts would care to enforce. The question of the legal enforceability of agreements is a matter for careful determination by legislators and by judges. If the Pennsylvania legislature passes a statute directing that a certain kind of agreement shall or shall not be enforced, the state judges are bound to obey that statute, provided it does not conflict with the state, or national Constitution or with Federal laws or treaties. In the absence of a constitutional or statutory provision and of a Federal law or treaty on a given subject, judges consult previous decisions in similar cases, and usually follow these old decisions, which are called precedents. Sometimes the courts refuse to follow ancient precedents. The law develops through the recognition by judges and legislators of the changing business necessities of the community. Certain kinds of agreements which are not now enforceable, because enforcement is not demanded by the economic situation, may in the course of time obtain legal recognition in response to such a demand.

The last part of the definition of a contract states that it is "made between two or more persons," and that "rights are acquired by one or more to acts or forbearances on the part of the other or others." A contract is essentially a binding personal agreement. The Latin word from which the English word "contract" comes means "to draw together." When people make a contract they tie themselves together by the terms of that contract. Take, for instance, an agreement between B, a book seller, and C, one of his customers, for the sale of a book. B offers a certain volume to C for a dollar, and C accepts the offer. B thereby binds himself to C for the

delivery of the book upon receipt of the price. C binds himself to B for the delivery of the dollar upon receipt of the book. A personal responsibility is assumed by each to the other. Each has a right against the other, and each is under an obligation towards the other. These two things, right and obligation, correspond with each other. They are correlative. The obligation of B to deliver the book fits into the right of C to receive that book. The right of B to receive the dollar matches C's obligation to pay it. B acquires by virtue of the contract a right to have C compelled, if legally possible, to do what he has promised to do, namely, to pay B a dollar. If B should be willing to deliver the book, but C should refuse to pay the dollar, B could get judgment against C, and the sheriff would be sent to sell C's property, if C has any property, in order to compensate B for C's breach of contract.

Suppose B has handed the book to C, but C has not yet paid the price. B has discharged his obligation to C, and, therefore, C's right to receive what was coming to him under the terms of the contract has been satisfied. The obligation of C to pay the dollar remains, and B's right to compel payment of the dollar remains also. Suppose, now, that C finally pays the dollar. His obligation has been fulfilled, and B's right under the contract has been satisfied. The contract ceases to fasten B and C together, for it has been fully performed. Neither party remains bound to the other by a contractual tie. B has the dollar, and his right is a right of property in that dollar, just as C's right is a right of property in the book. Before C paid the dollar B had no property right in any particular coin or bank note in C's pocketbook or safe. B had only a right against C personally arising out of C's promise to pay one dollar to B. When two people make a contract, the gist of the contract is the promise or promises given. The legal enforceability of the contract lies in the fact that the government, through the courts and the sheriff, will compel either party to make good his promise if the other party does likewise. When the promises are fulfilled, the contract is terminated. All rights arising under it have been satisfied and all obligations have been performed. The parties who were fastened together by the contractual tie are unloosed,

and they are again in the same situation that they were in before they ever thought of making the contract, so far as respects the personal relation between them.

CHAPTER II.

THE FIRST ELEMENT NECESSARY IN ALL CONTRACTS, OFFER AND ACCEPTANCE.

In the previous chapter it is stated that five elements are necessary in all contracts. These are: first, Offer and Acceptance; second, Seal or Consideration; third, Capacity of Parties; fourth, Reality of Consent; fifth, Legality of Object. If you find these five elements present you may be sure that you have a contract, except in the case of certain agreements which will be considered in the seventh chapter. If any of these five elements is lacking, you may be sure that you have not a valid contract. An entire chapter will be devoted to each element, and the present chapter will cover the first of the five, Offer and Acceptance.

It will be recalled that a contract is defined as "an agreement enforceable at law, made between two or more persons, by which rights are acquired by one or more to acts or forbearances on the part of the other or others." The first words of this definition show that a contract is an agreement, a voluntary meeting of the minds of two or more persons on a definite proposition. In order that the parties may reach this agreement, they must communicate with each other in some way. In virtually every case where two parties make an agreement, the process by which their minds come to the same point is by one party's proposing something, and the other party's accepting the proposal. There may be a quantity of correspondence, long negotiations and many propositions and counter propositions, but in almost every conceivable case the final coming together is effected by one party's making a certain offer, and the other's accepting it. At that moment

the meeting of the minds takes place, and, if the other elements are present, a contract is formed. One may fancy a case where two persons have been debating terms, but cannot quite get together, and a bystander suggests a happy compromise to which both persons simultaneously agree. In that case neither person can be said to have made the offer, for neither has advanced a proposition to which the other has acceded. Such an exceptional case, however, is of no great interest, because it does not disturb the theories upon which the rules of offer and acceptance rest.

Offer and acceptance constitute the very foundation of a contract, for you cannot have "an agreement enforceable at law" unless you have the minds of the contracting parties meeting in a definite understanding. This meeting occurs by the method of offer and acceptance. In legal parlance, the one who makes any offer is called the offeror, and the one to whom it is made is called the offeree. These terms are useful only in studying how the contract is formed, for if the offeree chooses to accept the offer, and the other elements are present, a contract arises, and it is usually of no importance afterwards to recollect which of the parties made the offer and which accepted it. Once the contract for the sale of a machine is formed, for instance, it can seldom make much difference whether the manufacturer of the machine offered it to the purchaser at a certain price and the purchaser agreed to take it, or the purchaser offered to pay a certain price for it and the manufacturer accepted that offer. However, in asking ourselves whether or not there has really been an agreement about a certain matter, we should follow the steps of the parties as they approach one another. If one makes a certain proposal, he is called the offeror with respect to that proposal, and the one to whom it is made is called the offeree. The offeree may reject the first proposal, and suggest something else more favorable to himself. As respects this second proposal he becomes the offeror, while the other party changes places with him and becomes the offeree. The two parties may continue negotiating indefinitely, but they do not reach any agreement until the offeree to whom a certain proposition is made accepts it. At the instant when the

offeror and the offeree fully come together on the same terms, you have offer and acceptance, and the contract is complete, if the other elements are present. The acceptance dovetails into the offer, and each holds the other fast.

Where the parties are talking face to face, and promptly come to an agreement, the first element, offer and acceptance, presents little difficulty. It is usually easy to discover whether or not their minds have definitely met on a certain proposition. On the contrary, where the parties are at a distance from each other, and keep up a desultory correspondence at long range, it is often hard to say whether or not their minds have met. The following rules may help the student who wants to learn if this element, offer and acceptance, is present in certain doubtful cases.

Rule 1.—The offer and acceptance must be definite.

The minds of the parties must come together on a substantial platform. When a man brings a lawsuit in the endeavor to enforce a misty understanding which has never been clearly defined by the parties, the courts cannot grant him any aid. There is no agreement to be enforced, and the courts will not make one for the parties. Men are free to make a contract or to refrain from doing so, and if they have not fully reached the point in their negotiations where they stand upon a common basis, the courts will not draw them together, and make them enter into a contract against their wills. The case of *MacMackin v. Timmins* (1884), reported in 14 W. N. C. 318, illustrates this idea. MacMackin & Young were organ builders. They entered into negotiations with Timmins, the rector of a church in Chester, for the construction of an organ. At the outset and throughout the interviews Timmins insisted on having a written agreement. At one interview Timmins authorized MacMackin & Young to go ahead with the organ, but at the same time demanded that all the terms of the agreement should be put in writing. Later, several forms of agreement were proposed, one by Timmins and others by the organ builders, but at last Timmins broke off all

negotiations. When he was sued for the price of the organ, the court sustained his contention that there had never been a contract. At no point in the negotiations had the minds of the parties met definitely, for Timmins had clearly indicated to the organ builders that he would not regard the agreement as complete until all the details should be settled and put in writing. Under ordinary circumstances, if a man orders an organ to be built there may be a contract without any writing and without the settlement of every petty detail, for if the minds of the parties have squarely met on a broad proposition, there may be a contract even though some trifling points have escaped their notice. As long, however, as one party withholds his assent, and indicates to the other party that he has not yet closed the contract, so long does the agreement lack that full meeting of the minds which is essential to the formation of a contract.

Another illustrative case is *Powers v. Curtis* (1892), 147 Pa. 340. Cyrus H. K. Curtis wrote to J. E. Powers, requesting him to prepare some leaflets for advertising the "Ladies' Home Journal," of which Curtis was the proprietor. Powers prepared a leaflet, and sent it to Curtis with this note: "\$100, if satisfactory." Not proving satisfactory, it was returned to Powers. Powers sent a second leaflet with a letter in which he said, "I put down in my book \$200 against you, but I'll wipe it all out if I can't suit you." Curtis then replied that the leaflets were good, but that he did not care to pay the prices asked by Powers, and added that he hardly needed any help in advertising the "Home Journal." Powers sued for his services, but the court held that the correspondence did not disclose a contract, the consent of two minds to a proposition. While Powers must have hoped to get paid for his work, yet his own letters showed that Curtis was not to pay him unless satisfied to do so. As Curtis had not agreed to accept the leaflets at the price named by Powers, there was no complete meeting of the minds, although it seemed that Curtis was satisfied with the quality of the advertisements.

This case makes it clear that courts will not redress every disappointment or fulfil every hope. The earnest, honest efforts

of a man in the same position as Powers may go unrewarded, but the courts cannot compel any person to reward them unless he has agreed to do so. Powers had only himself to blame for doing work in the mere expectation that it would please Curtis, and without a definite agreement that Curtis must pay for it. The decision in this case seems quite fair, because the government should not in such affairs take money from one man's pocket and put it in another's, unless the former has clearly agreed to pay the latter, and then wrongfully refused to live up to his agreement. In thousands of cases men go to expense and trouble in trying to induce others to make a contract with them. Architects spend days in drawing competitive plans in the hope that some land-owner who is about to put up a building will accept their designs, and engage them to supervise the building operation. They may be invited to prepare specifications, and encouraged to hope that they will be successful in gaining the appointment. Despite all this, unless the matter reaches the point at which the courts can see a definite agreement by the land-owner to adopt a certain architect's plans, there is no contract. The unsuccessful competitors have made toilsome preparations, each with the idea that he may be chosen, but preliminaries looking toward the formation of a contract are not enough to make a contract. Until the parties finally close upon a definite agreement, there is nothing for the law to take hold of and enforce. As a general rule, therefore, if one person has been led on by another in the hope that the other will enter into a certain contract with him, but that contract is never formed, the disappointed man has only his labor for his pains. He cannot ask the courts to fulfil his mere expectation which falls short of being a contractual right.

While the courts will not make an agreement for the parties if the latter have not made one for themselves, this does not mean that the courts are unreasonable and require the parties to express their terms with elaborate formality. Judges recognize that the agreements of business men are usually brief and to the point, and, therefore, they do not insist upon having all the terms set forth with the fullness of an international treaty. Many minor points are not mentioned at all in

some business agreements, for the parties know that these points are regulated by custom. If, therefore, it is clear that there has been a definite meeting of the minds, the absence of ceremony is usually of no consequence. The case of *Eckert v. Schoch* (1893), 155 Pa. 530, illustrates the common sense of the judges in looking at transactions from the standpoint of the parties themselves, and in not demanding unusual formality in the making of contracts. On April 10th, 1890, Schoch sent Eckert a postal card reading in part as follows: "If you can pay 83½ on track here for prime Pa. wheat will send you sample." Eckert received the postal on April 11th, and telegraphed back: "If stock good, think can place five cars price named. Send sample quick." A few hours later Eckert telegraphed again as follows: "Ship quick five cars prime red wheat to Stemton as trial lot." On the same day, April 11th, Schoch answered by postal: "I send you sample of wheat. I will ship you one car soon and if satisfactory will ship more." The first carload of wheat was duly forwarded, and Eckert repeatedly urged Schoch to send four more cars at once, to complete the contract. Schoch did not deny that the contract called for five carloads, and promised to send another car in a few days, but never did anything further in the matter. Eckert sued, alleging that there was a contract for five carloads, of which Schoch had delivered only one. The court declared that the only reasonable opinion to be formed from a reading of the entire correspondence was that the contract alleged had been entered into by the parties. Schoch, it is true, had never specifically promised to deliver five carloads of wheat, but an inspection of his notes to Eckert leads to the conviction that he expressed a willingness to accede to Eckert's terms. Schoch had opened the negotiations by quoting the price of wheat at 83½ cents per bushel. His postal of April 10th contained no legal offer, but only an invitation to a possible customer. Eckert was the offeror, for he offered to buy five carloads at the price suggested. Schoch, the offeree, accepted the offer by his postal of April 11th. The contract was closed then, and bound both parties. The subsequent correspondence, while it did not help to form the already closed contract,

throws light on the intention of the parties, for throughout Eckert refers to the agreement as covering five carloads, and Schoch seems to acquiesce in this view of it. One of the terms of Eckert's offer was that the quantity of wheat purchased should be five carloads, and the mere fact that Schoch had written about promptly shipping one car was not permitted to lessen the effect of his expressions which indicated a willingness to fill Eckert's order. If he had wanted to limit the agreement to one car, he should have so stated, and then Eckert might have backed out altogether, or perhaps might have chosen to make a contract for one carload of wheat. Schoch could not put himself in the position of agreeing to Eckert's proposition, and afterwards limit his delivery to one-fifth of the quantity called for by the contract.

You will notice that the price at which the wheat was agreed to be sold was fixed by Schoch's original quotation, and this was the basis upon which the parties entered into the contract. Schoch did not specify the price to be $83\frac{1}{2}$ cents per bushel. He used only the figures " $83\frac{1}{2}$," but those figures were sufficient to convey the idea to wheat traders that Schoch meant $83\frac{1}{2}$ cents per bushel, and judges do not insist upon the use of more words than are necessary to constitute a definite agreement. The courts will always insist, however, upon proof that there was a definite understanding between the parties, and the case of *Sherman v. Kit-smiller* (1827), 17 S. & R. 45, gives us an illustration of this rule.

Kit-smiller and another man were sued as administrators of the estate of George Sherman, deceased, upon a promise made by George Sherman to Elizabeth Sherman, to give her one hundred acres of land for acting as his housekeeper. This suit was brought for one hundred acres of land, and the following extracts from the court's opinion will show why it was decided that the alleged contract lacked the first necessary element, offer and acceptance: "If it had been a promise to give one hundred pieces of silver, this would be too vague to support an action. For what pieces? Fifty cent pieces or dollars? What denomination? One hundred cows

or sheep would be sufficiently certain, because the intention would be that they should be at least of a middling quality; but one hundred acres of land, without locality, without estimation of value, without relation to anything which could render it certain, appears to be the most vague of all promises, and if any contract can be void for its uncertainty this must be. One hundred acres on the Rocky Mountain, or in the Conestoga manor? One hundred acres in the mountain of Hanover County, Virginia, or in the Conewango rich lands of Adams County? One hundred acres of George Sherman's mansion place at eighty dollars per acre, or one hundred acres of his barren lands at five dollars?" The court mentioned, however, that the vagueness and invalidity of the agreement to convey one hundred acres to Elizabeth Sherman would not prevent her from recovering the money value of her services in another suit based upon an implied contract to pay for her work as housekeeper. Under the third rule about offer and acceptance we shall take up certain matters concerning implied contracts based on the conduct of the contracting parties.

Rule 2.—The parties must seriously intend to enter into an agreement.

The essence of any agreement is the meeting of the minds of the parties. If a man is talking in his sleep, and states that he will sell his house for \$1,000, and another man overhears the utterance, and calls back that he accepts the offer, there is obviously no agreement, for the sleeper's mind cannot be said to have met the mind of the other man. Likewise, if a man makes an offer by way of a joke, and the offeree snaps up the offer, and sues the offeror to compel performance of the alleged contract, the offeree cannot win his case if it appears that he had no reason to suppose the offeror to be in earnest. If the offeror, however, chooses to make a sham offer in jest, and gives the offeree to understand that he makes it seriously, and the offeree accepts in the belief that the offeror means what he says, there would be a contract, because the offeror should not be allowed to repudiate an apparent agreement on the

ground that he deceptively misrepresented his own state of mind. In the case of the ordinary bantering agreement, both parties understand that the words are spoken in a spirit of merriment without any accompanying mental intention to make a real agreement. It is the mind expressed through the words, and not the mere words themselves, that the courts look to; but there may be danger in jesting about any such matter. The other party may afterwards falsely or innocently swear that he took it seriously, and if he is believed he can enforce the alleged contract, provided the joke was so well carried out that it was likely to deceive an ordinary man. The circumstances surrounding a bantering agreement often help to show that the parties were not in earnest about it.

In the case of *Armstrong v. McGhee* (1795), Addison's Reports 261, Armstrong sued to recover a valuable horse from McGhee, on the ground that he had delivered the horse to McGhee by way of a joke. Armstrong had offered the horse to several persons for a trifle, and finally he offered it to McGhee for £5. The horse at the time was running lame after a hard ride. McGhee agreed to pay £5 for it, and took it off to his stable. Both parties lived in Greensburg, and were on intimate terms with each other. Some of the onlookers testified that they regarded the transaction as merely a piece of fun. McGhee claimed property in the horse, but the jury decided that he must have known that Armstrong had not seriously intended to sell the animal for £5, and that he was trying to overreach Armstrong, so the verdict was in the latter's favor.

The second rule on the subject of Offer and Acceptance is helpful in enabling us to distinguish between a genuine legal offer and a mere *quotation of prices*. Business concerns often advertise lists of prices at which they are selling various articles. These lists may be published in the newspapers, or mailed to individual customers, or spread broadcast in numberless ways. It cannot be imagined that the advertiser seriously intends to hold himself ready to enter into a contract with all the thousands of persons who may possibly decide to purchase a certain article at the list price. A bookseller, for instance,

may have only a dozen copies of a fine edition which he advertises for sale, but his advertisement may persuade a hundred customers to call for the work. Sometimes brokers, who quote prices on securities in circular letters which they send to investors, protect themselves in this matter by printing at the top of each circular: "Subject to prior sale, withdrawal or advance in price without notice." In most cases, however, even if this very wise precaution were omitted, the broker would not be held liable if a customer should want to insist on making the broker deliver the securities at the prices quoted.

It is not always easy to distinguish between a genuine legal offer and a mere quotation of prices. The terms in which a person couches a circular letter may prevent him from fairly arguing that he did not intend to enter into a binding agreement with anybody who might promptly demand the goods mentioned at the prices named. If the advertiser states that he has twenty articles of a certain kind to be sold at one dollar apiece to the first twenty customers calling for them, one to each customer, any of the first twenty customers would have a right upon asking for the article, and tendering a dollar in payment, to hold the offeror strictly to the agreement. On the contrary, if an advertiser should merely mention that he had articles of a certain description for sale at one dollar apiece, and a customer who wants the article is told that the advertiser had decided to hold the articles at two dollars each, the customer probably could not force the delivery to him of one of the articles at the advertised price. In the latter case, the merchant was merely quoting prices, and not signifying an intention to become bound in a contract with any person who might choose to give a dollar for one of the articles in question. In the former case, something more appears, for we can perceive a legal offer in the statement that the first twenty customers calling for the goods advertised may secure one of the articles for a dollar apiece. What is to be done when a dispute arises as to whether an alleged offer was really a legal offer to enter into a contract, such as could be accepted by any person to whom it was made, or was merely a quotation of prices? You should examine into the circumstances under

which the alleged offer was made, and find out the custom which prevails under such circumstances among those engaged in similar transactions. If a man who has duly accepted what he alleges to be a legal offer can prove that the advertisement or other communication of the alleged offeror was so phrased that it was reasonable to regard it as containing an offer, then there is a contract. On the other hand, if you write, for instance, that you have a quantity of rubber to sell at a certain price, and what you say would be regarded by rubber dealers as merely a quotation of prices, it would be unreasonable to let that quotation be seized upon by the man to whom it is made just as if it expressed an absolute legal offer to enter into a contract. Generally a quotation of prices indicates nothing more than a willingness to take up the matter of selling the articles mentioned with the idea of possibly forming a contract. It constitutes merely an invitation to negotiate on the basis suggested, but not an offer, which is the first half of the making of a contract, and which unites with acceptance to form a complete and binding contract.

On the same theory, if an architect advertises for *bids* he is merely inviting builders to negotiate with him and submit offers to him. He must not be considered as offering to enter into a contract with the lowest bidder, unless he expressly states that the award will be made to the lowest bidder. In the case of *Leskie v. Haseltine* (1893), 155 Pa. 98, it was proved by Leskie that he had been specially invited to bid by Haseltine, who was about to put up the Haseltine Building, in Philadelphia. He contended that it was customary under these circumstances for the lowest bidder to be chosen. The right to reject any bid had not been expressly reserved by Haseltine. Leskie testified that when the bids were opened Haseltine said to him, "You are the lucky man." Despite all this, it was decided that there was no contract between the parties, and that Haseltine might award the work to any person he chose to select. The words, "You are the lucky man," amounted to nothing more than a recognition of the fact that Leskie was the lowest bidder. Haseltine, when he invited bids, was not an offeror, but was merely soliciting offers. It is

wise, nevertheless, to insert in invitations for bids a term providing that any or all bids may be rejected, because such a term may forestall disputes and litigation. Under the sixth rule we shall see more about the legal character of bids.

The rule that the parties must seriously intend to make a definite agreement applies also to many *advertisements* which promise that medicines or other goods advertised will give the purchaser wonderful results. The phrase, "cure guaranteed," catches the eye in many advertisements of patent medicines. If the purchaser of a box of pills, which are advertised as being a "warranted one night cure" for hay fever, uses the pills without getting the desired relief, he has no right to sue for compensation for his subsequent sufferings on the ground that the medicine was really guaranteed to prevent them. The ordinary reasonable man who reads a medicine advertisement understands that the advertiser often extravagantly puffs up the value of his goods. It cannot, therefore, be reasonably asserted that the parties seriously intended to include in the contract for the sale of the pills a guaranty that they would surely possess all the magical powers claimed for them, and promptly restore the suffering purchaser to the best of health. Suppose, however, that the advertiser states that he has deposited in a certain bank \$1,000 out of which any purchaser of the pills, who may not become cured, will be reimbursed for whatever doctor's bills he may incur within one month after unsuccessfully trying the pills. This statement would indicate a serious intention, and a disappointed purchaser could recover from the advertiser the amount paid to his doctor for treating, during the time named, the hay fever which the pills failed to cure.

Rule 3.—The offer or the acceptance or both may be made either by words or by conduct.

This third rule about offer and acceptance is subject to some exceptions in the case of certain contracts which require special formality. These will be considered in the seventh chapter. As a general proposition, however, it is true that no writing and no special words are required to make a contract,

and that conduct which clearly indicates the intention of any party to enter into a contract is equivalent to the words which he might employ to express that intention. Usually the law disregards form, and looks at substance. The essence of a contract is the meeting of the minds of the parties, and their minds may communicate together by word of mouth or by deaf and dumb signs or by any conduct which conveys the intention to make an offer or to accept it. Suppose a bookseller displays a number of volumes in his window. If a customer enters the store, selects one of the volumes, hands it to a salesman to be wrapped up, and finally puts it under his arm and walks away, there is clearly an acceptance of the offer to sell the book. Not a word may have passed, but the bookseller has a right to sue the customer for the price of the volume, just as well as if there had been a verbal or written agreement on the subject.

In the case just mentioned both the offer and the acceptance are gathered from the conduct of the parties, the bookseller and his customer. Sometimes only the offer is made in words, and the acceptance is implied from the conduct of the offeree. Again, sometimes the offer is to be implied from the conduct of the offeror, and the acceptance of the offeree is conveyed by language expressing his intention to accept. The agreement of the parties is what binds them together in a contract; and if this agreement is sufficiently communicated, the failure to employ words for that purpose is not fatal.

Needless to say, it is preferable to have a contract made in express words rather than by conduct, for the meaning of the parties can usually be conveyed more accurately by language than by their silent actions. In the same way, it is preferable to have the terms of an agreement put in writing, for a written contract is usually more clearly expressed than a verbal one, and its terms are more easily proved when difficulties arise and proof becomes necessary. This does not conflict with the rule, however, for it only shows that it may be more satisfactory to have a contract fully expressed in words, than to depend upon the conduct of the parties for proof of their intention to form a contract. Where their conduct is open to only one reasonable interpretation, namely, that they intended to make a con-

tract, the contract is just as enforceable in most cases as if it were put in writing. If a stranger jumps into a hansom at a railroad station, and calls out the name of a hotel to the driver, and the driver takes him to the hotel, the passenger must pay his fare. The acts of the parties prove that they have formed a contract, by which the passenger is bound to pay for his transportation. Again, if a man takes a newspaper from a news-stand, and goes off with it, he binds himself by a contract to pay for the paper. On the contrary, if a lad offers cards advertising a neighboring restaurant to passers-by on the street, one of whom accepts a card, there is no contract formed by which he becomes liable to pay anything for the advertisement. The difference between the last two cases is that the person who takes the newspaper must be understood, in accordance with ordinary common sense, as agreeing to pay for it, while, on the other hand, the man who accepts the advertisement cannot reasonably be supposed to agree to pay anything at all for it. The courts regard these matters from the standpoint of the average sensible person, and decide that a contract has been formed if it is natural and proper to draw that inference from the conduct of the parties. If a man wants to make a contract with another, it is safer not to rely entirely upon the other's conduct, for sometimes conduct is open to more than one explanation. Many persons do favors for others entailing hard work with no expectation of being paid, and one who has received a favor will not be compelled afterwards to pay for it, if it is not shown that the parties must have so intended when the work in question was performed.

The courts are quite reluctant to infer a contract from mere conduct *where the parties to the alleged contract belong to the same family*, and there is an attempt to establish an agreement to pay for services rendered by one member of the family to another. Relatives perform thousands of kind services for one another without any expectation of receiving money, and courts will not make the beneficiaries account for the value of every friendly act. The closer the intimacy of persons, the more freely do they aid each other without any idea

of a contract to pay. Relatives who share the same home will help one another in many matters without a thought of being paid, although they would expect compensation for similar work if they lived apart in distant towns, and rarely corresponded. In many cases where a claimant seeks to recover money for services rendered to a relative, it is hard to discover whether or not there was an understanding to be derived from all the circumstances that the services should be paid for in cash. Two cases reported in the law books will help us to draw the line between purely gratuitous services and services for which payment may be fairly expected.

In *Lafferty's Estate* (1892), 2 D. R. 205, the Orphans' Court dismissed a claim against a dead man's estate for his niece's services as nurse and housekeeper. The niece alleged that there had been an implied contract between her uncle and herself, but she proved neither an acknowledgment by the decedent of indebtedness to her, nor any demand for payment during his lifetime. Where a claimant delays a long time before presenting the claim, its staleness casts suspicion on it. In this case, besides, the close intimacy and relationship of the parties tended to negative any presumption of an implied contract. The niece had expected that her uncle would recognize her kindly services and attentions by a legacy, but this fact told against her alleged contract rather than in favor of it. If there had been an express agreement that payment was to be made out of the uncle's estate, there would have been a contract, but the niece's expectation that her uncle would make her a handsome gift in his will pointed to the probability that her services had been rendered gratuitously in the hope that the uncle would deal as generously with her as she had dealt with him. When the return for services is left entirely to the generosity of the man who gets the benefit of them, the transaction is on the basis of pure gratitude, not on the basis of contractual liability enforceable at law.

The case on the other side of the line is that of *Young's Estate* (1885), 32 Pitts. L. J. (O. S.) 403. A man who lived with his own family at a distance from his father's home was sent for by the father, who asked him to collect certain rent.

The son had considerable trouble in forcing one of his father's tenants to pay, and while he was endeavoring to collect the money the father died. The son afterwards recovered \$365 from the tenant, and made a claim against his father's estate for the value of his services. It was allowed on the ground that the services were of so burdensome a nature that they would not ordinarily be rendered free of charge by a son who had his own family to look after, and who was living apart from his father. If the son had been asked by a stranger to perform similar services, and had done so, the presumption would clearly be in favor of a contract to pay for the services. He did the work, however, for his father, and this case is noteworthy, because usually where a son performs services at his father's request, the law presumes that the father is not to pay anything, unless a distinct agreement by the father, or his past course of dealing with the son, shows an understanding that the latter is to be paid. Likewise, where two persons are not connected by ties of blood, but one really occupies the position of a father to the other, services rendered by one to the other are supposed to be gratuitous, unless there has been an agreement to pay for them, or unless they are rendered under exceptional circumstances, as in the case of *Young's Estate*.

We have been looking at the question as to whether or not an implied contract arises from the performance of services by one person at another's request. The theory upon which the courts make out a contract in some of these cases is that a request for the performance of services usually carries with it an implied promise to pay for them, except sometimes among friends and relatives. The man who merely asks another to perform services for him is usually to be understood as tacitly offering to make proper compensation for the services. He is the offeror, and the man who does the work is the offeree, and accepts the offer. Suppose, now, that a man performs certain services for another without being asked to do so. It is clear that he cannot recover money for them, for he cannot pretend that there was any contract to pay for them. *One is not permitted to thrust his services upon another, and force the latter to pay for them.* Unless the courts can deduce from a

man's words or conduct that he has agreed to pay for certain work, the mere doing of the work, which benefits the man himself or his property, gives nobody a right to demand payment from him. If, however, a servant is employed for a month, and continues in his master's home from month to month, always receiving wages for his work, the master could not refuse to pay at the end of any month on the ground that he had not asked the servant to stay with him. The mere acceptance of the services would indicate an intention to pay for them in view of the prior employment.

In general, therefore, when one is faced with a difficult problem on this topic of contract implied from conduct, it is best to put one's self in the place of the average reasonable man, and to ask if an intention to enter into the alleged contract is reasonably deducible from all the facts and surrounding circumstances. There are many neighborly acts which the average man will do for his acquaintances without any thought of pay. There are many courtesies which are extended to utter strangers. On the other hand, there are numerous services which a man could not reasonably expect even a friend to do for him without a definite idea of getting paid their fair value.

Rule 4.—An offer is not made until it is communicated to the offeree.

Everybody knows that you do not make a legal offer if you utter the words of an offer out of the hearing of any human being. Likewise, if you write a letter containing an offer, and address it to the offeree, but change your mind at once, and destroy the letter, you have never made a legal offer. You incur no liability, and even if you were to describe what you had done to the offeree, explaining to him that you had changed your mind before sending the letter, he could not hold you to any contract by declaring that he would accept the offer. The offer never had any legal existence, for it is not made until it is communicated to the offeree.

This rule applies in the case of public offers to pay rewards for the return of lost articles, or for the arrest and conviction

of criminals. Where notices offering a reward in such matters are posted about, the man who promises the reward is the offeror, and the entire public is the offeree. Any person who learns of the offer and does what the offeror wants may claim the reward. Suppose a general public offer to pay \$1,000 for the arrest of an escaped convict is advertised, and a man who has captured and brought back the convict before learning of the offer claims the money. He recognized the convict's prison garb, and arrested him out of a sense of duty. He has no right to get the reward, for there was no contract between him and the man who offered it. There was no meeting of the minds upon the proposition that the money should be paid for the return of the convict. The work of capturing the convict was done gratuitously, and the man who did it cannot recover either the amount of the reward on the theory of a contract to pay \$1,000, or even the ordinary value of his services and time, for what he did was done voluntarily.

Rule 5.—Acceptance must be communicated to the offeror, but it is legally communicated when made in the manner demanded or indicated by the offeror, even though it does not actually reach the offeror.

From the fourth rule we learn that the first step towards the formation of a contract is not taken until the offer is actually communicated to the offeree. The fifth rule, which we are now taking up, concerns the communication of the offeree's acceptance. It is not enough for the offeree to determine within the hidden recesses of his own brain to accept the offer. Some outward indication of his intention to accept must be given before the contract is formed. Fairness to the offeror requires that he should not be bound until the offeree does something to communicate the acceptance to him. Imagine, now, that the offeror has sent his offer by a messenger, and has stated to the offeree that the messenger is to carry back the answer. Suppose the offeree accepts, and the messenger is going back with the letter of acceptance to the offeror, but loses it, and runs away to escape the offeror's anger. The offeror does not receive the letter, and, supposing that the offeree does

not intend to accept, he goes ahead to make other arrangements with third parties. Later he happens to meet the offeree, who states that the contract has been closed, and that the offeror must live up to it. Which of the two parties shall suffer by reason of the miscarriage of the letter? The offeror must suffer, for the offeree has communicated his acceptance in the manner demanded by the offeror. The offer was accepted, and the contract formed at the moment when the offeree delivered the acceptance to the offeror's messenger. Comparing the fifth rule, which we are now studying, with the fourth rule, we see that while the offer is not made until it is actually communicated to the offeree, on the contrary the acceptance may be legally made before it is actually communicated to the offeror. Since the formation of the contract takes place when the offeree communicates his acceptance in the manner named or indicated by the offeror, it follows that if the messenger designated by the offeror never delivers the acceptance to the offeror, there is a contract none the less.

In the chapters which deal with Agency, we shall treat that subject at length. It may be stated here that if a man appoints an employee as his agent to receive offers, an offer communicated to this agent is legally made at the time it is so communicated, although the employer never learns of it. The offer, however, even in that case must actually come to the knowledge of the agent, before it is legally made. In the cases we are now considering concerning the communication of the offeree's acceptance, we can see that there is not always the same necessity for the communication of the acceptance to the mind of the offeror or of the offeror's agent. The case mentioned above, in which the offeror's messenger never delivered the acceptance, illustrates the possibility of the legal communication of acceptance, even though actual knowledge of the contents of the letter of acceptance does not come to the mind of the offeror or of his messenger. In that case the offeree did all that the offeror suggested to communicate the acceptance, and he could not be blamed if the acceptance was not in fact made known to the offeror. The point is that, while certainly the offer is not a legal offer until it is

actually made known to the offeree or his agent, the acceptance may in some cases be a complete legal acceptance even though it never actually reaches the offeror or his agent. If the offeror instructs the offeree to signify his acceptance by firing a gun at a certain time and place, and the offeree complies with these instructions, he may hold the offeror bound by the contract, although nobody but the offeree himself hears the report of the gun. There was a meeting of the minds of the two parties, and the offeree has communicated his acceptance in the way desired by the offeror.

The case of *Barney v. Clark* (1874), 22 Pitts. L. J. (O. S.) 69, introduces us to another phase of the same situation. Clark & Smith mailed a letter to Barney, Demoss & Co., offering to pay a certain sum for a certain quantity of oats. The offerees wrote a letter, properly directed to Clark & Smith, accepting the offer, and deposited it in the post. Clark & Smith afterwards denied that they had received the letter of acceptance, and refused to take the oats, asserting that no contract had ever been formed in the matter. Barney, Demoss & Co. were allowed to recover damages from Clark & Smith on the ground that a contract had been formed the instant when the letter of acceptance was mailed. The theory upon which it was decided—that a contract arose at the moment of mailing the acceptance—rests upon the fact that Clark & Smith had used the U. S. postal department as the means of conveying their offer. Thereby they indicated that the mails would be the proper channel for the communication of the offerees' acceptance, and as soon as the offerees adopted the tacit suggestion to deposit their acceptance in the post, they had done their part, and the contract was completely formed. In just the same way, if an offer is telegraphed, and the offeree telegraphs back his acceptance, the contract is formed at the moment when the telegram of acceptance is delivered to the telegraph company. The offeree has done what the offeror impliedly suggested to communicate the acceptance, and the contract is enforceable, even though some accident prevents the delivery of the telegram to the offeror. If the offer was made in the course of a talk between the parties, and the offeree afterwards

decides to accept it, and mails or telegraphs his acceptance, but the acceptance never reaches the offeror, there is no contract. Unless the offeror has said or done something to induce the offeree to communicate acceptance in the manner adopted by the offeree, the latter must bear the risk of the miscarriage of his acceptance.

The offeror has a right to stipulate that the offeree shall communicate the acceptance in a certain manner, and if the latter disregards this term of the offer the offeror may refuse to treat the contract as having been formed. If, for instance, the offeror makes his offer by mail, but states that the acceptance must be telegraphed back, the offeree cannot hold the offeror unless his acceptance is telegraphed. Again, if the offeror sends a printed form to the offeree, and declares that the acceptance must be made on that form, any other kind of acceptance is insufficient, and the offeror may refuse to recognize the existence of a contract.

In the third rule it is stated that the acceptance may be made by conduct, and where the parties are dealing face to face, the act of the offeree in performing the work which the offeror wants done is conduct which shows his intention to accept the offer. If a man orders a meal in a hotel, compliance with that order by serving the meal to him is certainly sufficient communication of the hotel-keeper's acceptance of the offer to buy the meal. Where the parties are not face to face, it is usually safer for the offeree to do more than perform what the offeror wants him to do. He should promptly notify the offeror of his intention to accept. See the case of *Emerson v. Graff* (1857), 29 Pa. 358. Emerson signed an agreement to pay any loss which Graff might sustain if Graff took twenty shares of Pennsylvania Railroad stock. Graff subscribed for twenty shares, and sued Emerson to recover the loss he suffered by doing so. The court refused to hold Emerson liable, because Graff had bought the shares without notifying Emerson. He had intended to accept Emerson's offer, but had not promptly communicated his acceptance. The mere purchase of the shares from a third person was not sufficient to notify Emerson that his offer had been accepted.

In the case of public offers, as, for instance, where a reward is advertised for the recovery of a lost horse, it is out of all reason to expect that any person who may claim the reward should first notify the offeror of his intention to look for the horse, and then hunt for it and claim the reward, if the search is successful. In such case the return of the horse is sufficient communication of the finder's intention to accept the offer, and earn the reward. The following case will show that the courts take a reasonable view of what is proper under such circumstances, and that they are not unduly strict in requiring express notice of acceptance in every case, where the offeror has not stipulated for it. In *Hoffman v. Railroad* (1893), 157 Pa. 174, it was proved that Hoffman had offered to give a right of way across his farm to a railroad company which should undertake to construct a line running into Sullivan County. Other farm owners made similar offers, and the board of directors of a railroad company passed a resolution accepting all such offers. The company began work upon the line which it mapped out through Hoffman's farm, and spent considerable money in the work. Hoffman contended that no contract had ever been completed between the railroad company and himself, asserting that the company's intention to accept his offer had never been communicated to him. The court decided that it was quite natural and proper for the company to communicate acceptance by starting work on Hoffman's farm, and that no verbal or written notice to Hoffman was necessary to complete the contract.

In applying the fifth rule to cases like *Hoffman v. Railroad*, the best way to test the matter is by asking whether or not the offeree's conduct was sufficient to give reasonable notice of his intention to accept to the offeror. In many such cases the offeree's conduct in starting the work desired by the offeror is so openly visible that an ordinary reasonable man should observe it and infer from it the offeree's intention to accept the offer. The offeree's acceptance is sufficiently communicated in this way, unless the offeror has demanded an explicit verbal or written acceptance. It is usually safer, however, and always more business-like, for the offeree to give an explicit

acceptance, and not to rely upon the communication of his acceptance by means of the notice to be derived from his conduct in going ahead with the work wanted by the offeror.

Rule 6.—An offer creates no legal rights unless it is accepted, and it may be revoked by the offeror at any time before acceptance.

A man is free to make or not to make an offer. If he chooses to make it, he may withdraw it at any time, unless it has been previously accepted. After the offeror has withdrawn it, the offeree cannot accept, for he is too late. This rule is perfectly fair, because the offeror should be free to revoke the offer, just as the offeree is free to reject it, unless the offer has been accepted. Up to the moment of acceptance neither party is bound to the other. At the moment of acceptance the contractual tie is knit, and both the parties are bound together by it. No matter how long they have been negotiating, either party is free to break off negotiations if no contract has been made. Likewise, if the offeror makes an offer, and straightway regrets having made it, and withdraws it the next second, the offeree cannot accept it a minute afterwards. The fact that the offeree was not given any time to consider the offer makes no matter.

The case of *Bosshardt & Wilson Co. v. Crescent Oil Co.* (1895), 171 Pa. 109, shows that this rule will be strictly applied. On July 31st, 1893, Crescent Oil Co. wrote to Bosshardt & Wilson Co., offering to supply oil up to 400,000 barrels at a certain rate, and stating that the refusal of the contract on the terms outlined was extended for the term of sixty days from date. On September 26th, Crescent Oil Co. withdrew the offer, but on September 27th Bosshardt & Wilson Co. wrote to accept it, and denounced the attempted withdrawal of it. During the summer Bosshardt & Wilson Co. had made preparations to do an extensive business, expecting to get oil in accordance with the offer of July 31st, and the withdrawal of that offer entailed the most serious financial trouble upon the offeree. Nevertheless, the court decided that the offeror was free to revoke at any time before acceptance, even

though it had promised to hold the offer open for sixty days. In *Huber Co. v. Smithgall* (1902), 19 Super. 641, and *Car Co. v. Stamm* (1904), 207 Pa. 419, one can study the difference between a mere naked *offer*, which is revocable until accepted, and an *option* which cannot be revoked by the party giving it because supported by a consideration from the other party or by a seal.

The case of *Fisher v. Seltzer* (1854), 23 Pa. 308, gives us a further insight into the operation of the sixth rule. Fisher was the sheriff of Lebanon County, and put up certain land at public sale. Seltzer bid \$7,000 for the land, thinking that it would be sold clear of all liens, although the land really was put up for sale subject to a \$6,000 mortgage. Seltzer quickly learned of his mistake, and at once withdrew his bid, but the sheriff knocked the property down to him. One of the conditions under which the sheriff put up the property was that "no person shall retract his bid," and another condition was that if the purchaser should retract his bid or should fail to comply with the conditions he should pay all costs and charges. Seltzer refused to take the land, and the sheriff put it up for sale another day, and sold it to another person for \$1,500. Seltzer was sued for the costs of the second sale and also for \$5,500, the difference between \$7,000 and \$1,500. The court held that mutuality is essential to a contract of this kind. A bid at auction before the hammer falls is a typical instance of an offer before acceptance. Seltzer had the right to withdraw his bid at any time before the property was struck down to him, and the sheriff could not prescribe a condition which would deprive him of that right. As the bid had been, therefore, legally withdrawn before acceptance, there was no contract, and Seltzer could not be regarded as a purchaser. Accordingly, he was not liable for the sum of \$5,500 or for the costs and charges of the second sale.

The situation would, perhaps, have been different if there had been an unofficial auction of the property, previously advertised as an absolute, unconditional auction, without reserve. If it had thus been understood that the highest bidder would have an absolute right to take the property, the highest bidder would, perhaps, be regarded as accepting the offer made to dispose

of the land to the person who should bid the largest sum for it. The highest bidder would be the offeree in that case. At the ordinary auction sale the highest bidder is an offeror, and the acceptance of the offeree is indicated by the words or actions of the auctioneer who is acting for the owner of the property. Let us look at this distinction more closely. At sheriff's sales, as in the case of *Fisher v. Seltzer*, and at most unofficial auction sales, the property may be withdrawn at any time before acceptance of the highest bid. This means that the property is put up at auction merely to invite bids, and there is no obligation to accept the highest bid. The person who has the property put up does not, therefore, stand in the position of an offeror, for he is merely seeking an offeror, that is, seeking a person who will make a good offer for the property. The bidders are all offerors, and the offer of the highest bidder may be accepted or rejected at the pleasure of the offeree. In a special case, on the contrary, where it is agreed that the highest bidder shall have an absolute right to receive the property for the sum he bids, the owner of the property, who makes such an offer, is the offeror. He has agreed to sell without reserve, and the man who makes the highest bid at the auction is an offeree, and accepts the offer by making the highest bid. This is an exceptional case, for most auction sales are made without the understanding that the property shall be sold unreservedly to the highest bidder. At most auctions, therefore, the auctioneer may refuse to sell to the highest bidder, and the highest bidder has the privilege of revoking his offer until the auctioneer accepts it. At the root of the idea of most contracts lies the thought that both parties are bound together, each to the other. It would be unfair to hold the highest bidder bound until the auctioneer has bound the owner of the property by his acceptance of the highest bid. At the moment of acceptance both parties become bound simultaneously.

The rule that an offer may be revoked at any time before acceptance enables the offeror to cancel an offer which he has made by mail, if he can communicate with the offeree before the latter accepts. The offeree's acceptance and the closing of the contract date in such a case from the time when the offeree

drops his letter of acceptance in the post. The offeror must notify the offeree of his revocation before the contract is closed, otherwise the attempted revocation is too late. The offeror should telegraph or telephone as soon as he makes up his mind to revoke. Suppose an offer is made by a New Yorker, and his letter reaches Chicago, where the offeree lives, on March 10th. The Chicagoan mails his acceptance on March 10th, and it does not reach the New Yorker until March 12th. On March 11th the New Yorker has mailed a letter of revocation with a special delivery stamp, and it so happens that the letter of revocation actually reaches the Chicagoan before the letter of acceptance reaches the New Yorker. The revocation is, nevertheless, too late, because the contract was closed at the instant when the letter of acceptance was posted in Chicago. The revocation is not legally communicated to the offeree until he actually receives it, and does not date from the time it was mailed by the offeror. In accordance with the fifth rule, communication of the acceptance was legally made at the time the letter of acceptance was mailed. If, on the other hand, the offer has been made verbally, and the offeree mails his acceptance, the contract is not closed until the acceptance is actually received by the offeror, and if the offeree is notified of the revocation before his letter actually reaches the offeror, there is no contract.

The case of *McKee v. Harris* (1883), 40 L. I. 232, is another example of the working of the sixth rule. McKee had been corresponding with Harris about buying the latter's house. On November 27th, 1882, he had written to Harris, accepting an offer which Harris had made. His letter was not mailed, but McKee himself took it to Harris on November 29th. Harris declined to receive the letter, and at the trial swore that he had told McKee, when the latter first appeared in sight on November 29th, that he had decided not to sell. McKee swore that the revocation was made after Harris had been notified verbally of McKee's acceptance. The court refused to compel Harris to convey the house, because, if his own story were believed, he had notified McKee of his revocation before McKee's acceptance had been communicated to him. In the

ordinary case, where you have oath against oath, and the plaintiff is only asking for money damages, the court will leave the disputed questions of fact to a jury's decision. Where, however, the court is asked to give extraordinary relief to a plaintiff like McKee, who wants to compel the defendant to convey real estate to him, the court will refuse to grant the relief, if the oath of the defendant squarely meets that of the plaintiff, and the plaintiff offers no other evidence.

Rule 7.—An offer, if not accepted within a reasonable time, will lapse, and cannot be accepted thereafter.

The courts understand that the offeror does not intend to keep his offer open forever, although he does not withdraw it or say anything about the length of time during which the offeree may accept. If the offeror specifies a certain time during which the offer is to hold good, it will remain good during that time, (unless withdrawn by him), and not a minute longer. Assuming now that no time has been mentioned, and that there has been no revocation by the offeror, the question is, "How soon must the offeree accept?" He has a reasonable length of time, varying with the particular circumstances. In the case of ordinary business transactions, men are supposed to make up their minds quickly, and the offeree should usually accept the same day that the offer reaches him. This is very evident in the case of offers to sell perishable goods or goods whose price fluctuates rapidly. Indeed, where an offer is made to buy or sell stocks on the floor of a stock exchange it is usually understood that the acceptance must be made instantly, otherwise the offer lapses, and a subsequent attempt to accept comes too late. There cannot be a meeting of the minds of the parties, for the mind of the offeror is no longer open to admit an acceptance. Certainly, if the offeror is still willing to close the contract, he is at liberty to do so, and he may be glad to receive a tardy acceptance. The point is this, that the offeree who tries to accept after the offer has lapsed cannot compel the offeror to make the contract.

A delay which would be unreasonable under some conditions may be proper under other conditions, and in the latter

case the acceptance is not too late. The case of *Hoffman v. Railroad* (1893), 157 Pa. 174, presented circumstances which made the court decide that a delay of over three years in accepting was not too great. We saw this case under the third rule. Hoffman and other land-owners had made certain offers looking to the building of a railroad line across their farms. The Railroad Company finally accepted these offers, but Hoffman objected that the acceptance came after his offer had lapsed. The court held that from the nature of the work to be done, it was evident that the time required to organize the contemplated company, and to raise the money necessary for the enterprise, would be considerable. Hoffman was not offering to sell a portion of his perishable crops. He was arranging for the building of a costly and permanent railroad line, the laying out of which demanded extensive surveys. He understood that the company had not been fully organized at the time his offer was made, and that there would be a great deal of tedious detail work to accomplish before the projected railroad could be got under way. The delay in this case was very long, but it was satisfactorily explained.

Shaub v. Lancaster City (1893),¹ 156 Pa. 362, is another case under the seventh rule. In 1874 the councilmen of Lancaster passed a resolution directing the mayor to offer a reward of \$500 for the arrest and conviction of anybody setting fire to buildings within the limits of the city. In 1874, and again in 1879, the incumbent mayor published a notice offering the reward. In 1891 Shaub secured the arrest and conviction of a man who had just caused an incendiary fire. The city authorities refused to pay him the reward, and the court decided against Shaub, explaining that the offer had lapsed. The following quotation is from the court's opinion:

"We must regard the resolution of 1874 as an act done in the transaction of the business of the city that was not intended to bind the city longer than the condition which suggested its adoption should continue. The property of citizens and the welfare of the city were in danger from incendiary fires. The ordinary measures for the detection and conviction of criminals seemed to be inadequate to meet the necessities of the situa-

tion. Additional and extraordinary methods were thought necessary, and to secure these a reward was offered to any person who should detect and procure the conviction of an incendiary. It was not a permanent law of the municipality, but a temporary order to meet a temporary necessity. When its work was done it required no formal repeal or rescission to terminate its operation. It expired. For a reasonable time to accomplish its original purpose it must be binding. Beyond such reasonable time it cannot be. It is difficult to lay down a rule that should be more definite or precise than this, and each case must stand on its own circumstances. Ordinarily such a resolution ought not to be acted upon, except by the mayor to whom the order is directed, nor ought its terms to bind the city beyond the term of such officer; but the only general rule that it is safe to lay down is that the terms of the proclamation cease to bind the city after the lapse of a reasonable time; and in determining what is a reasonable time the reason or necessity for the action must be taken into account."

Rule 8.—The offeror's death revokes the offer.

If the offeree has not accepted before the death of the offeror, his attempt to accept thereafter is ineffective. There can be no meeting of the minds after the offeror dies. Even though a reasonable time has not been given to the offeree, even though the offeror has promised to hold the offer open for a long period, the offeror's death terminates the offer at once. In the third chapter we shall see that the offeree who wants to protect himself by having the offer kept open for a certain time, may do so by securing a legal option from the offeror. An option is better than a mere naked offer, for it survives the death of the offeror, while the offer expires with him.

Rule 9.—Acceptance cannot be presumed from the silence of the offeree or from his delay in rejecting the offer.

The offeree may say nothing when a verbal offer is made to him, or he may declare that it sounds like a good offer and that he would like time to consider it. In neither case does he

accept the offer, and if he keeps begging indefinitely for more time to make up his mind, he does not legally come any nearer acceptance than he was in the beginning. No mere hesitancy on the offeree's part as to whether or not he shall accept the offer can be construed into a definite acceptance. Until there is a definite acceptance, there is no contract, and neither party is bound.

The case of *Insurance Co. v. Beatty* (1888), 119 Pa. 6, emphasizes this rule. Beatty had two fire insurance policies on certain property. The policies expired January 6th, 1886. On January 5th, a man who was looking after Beatty's insurance went to the insurance company's office to have the policies temporarily kept in force. This man had other business to transact at the company's office, and he first asked the renewal clerk to extend the term of Beatty's two policies, and then discussed his other business with the clerk. The latter said nothing and did nothing regarding Beatty's policies, but Beatty's agent assumed that the renewal clerk agreed to extend them. On January 10th Beatty suffered a fire loss which the insurance company refused to make good. The Supreme Court said, "We find ourselves unable to discover any evidence of a contractual relation between the parties to this litigation. The contract alleged to exist was not founded upon any writing, nor upon words, nor upon any act done by the insurance company. It was founded alone upon silence. While it must be conceded that circumstances may exist which will impose a contractual obligation by mere silence, yet it must be admitted that such circumstances are exceptional in their character and of consequently rare occurrence. But in any point of view, it is difficult to understand how a legal liability can arise out of the mere silence of the party sought to be affected, unless he was subject to a duty of speech, which was neglected to the harm of the other party. If there was no duty of speech there could be no harmful omission arising from mere silence. The hearing of a request, and not answering it is as consistent, indeed, more consistent with a dissent than an assent. If one is asked for alms on the

street, and hears the request, but makes no answer, it certainly cannot be inferred that he intends to give them."

Rule 10.—The offer lapses if the offeree rejects it, or makes a counter proposition.

If the offeror makes a certain proposition, and states that he will keep it open for ten days, but the offeree straightway rejects it, the offer lapses. The offeree cannot within the ten days change his mind, and compel the offeror to stand by the offer, if the offeror is no longer willing to do so. Even though the offeror promised to hold the offer open for ten days, the subsequent refusal of the offeree leaves the offeror free to regard the incident as closed. The offer ceases to be operative. Likewise, if the offeree makes a counter proposition, the original offer lapses. The counter proposition implies that the offeree declines the original proposition, and wants to do business on other terms.

The case of *Bower v. Blessing* (1822), 8 S. & R. 243, illustrates the rule. In the course of a lawsuit Blessing filed a paper, by which he declared "that in case the verdict should be in his favor, he agreed that referees should be appointed by the court." These referees were to determine certain matters in connection with the verdict. The verdict was given by the jury in favor of Blessing, but Bower did not make arrangements to have the referees appointed. Instead, he applied to the court for a new trial. His application was refused, and then he turned around, and demanded that the referees suggested by Blessing be appointed. His acceptance of the offer to appoint referees came too late, because his application for a new trial implied a rejection of the offer to have referees appointed, and the offer thereupon lapsed.

Rule 11.—The acceptance must be absolute and identical with the terms of the offer.

A contract is an agreement which two or more persons freely make. It would be wrong to hold the offeror to terms which are different from those to which he has consented. If the offeree does not come to terms, but hangs back a little

short of acceptance, there is no contract. He must accept absolutely. If he declares that he probably will accept, this amounts to nothing, so far as the formation of a binding contract is concerned. If he says that he will accept, but demands new terms and conditions, he is really not accepting. He is making a counter proposition. Until the minds of the parties have fairly met there is no contract.

The case of *Vincent v. Oil Co.* (1895), 165 Pa. 402, illustrates the point that the acceptance must be absolute. Vincent sued for commissions on the sale of an oil lease, and the defense was that his authority had been withdrawn before he had effected a sale. One Wednesday Vincent telegraphed the Oil Company that a prospective purchaser would examine the property on the following Friday. The same Wednesday the Company telegraphed back that Vincent must send them an answer before that night. Vincent telegraphed back, "I leave to-night and consider trade closed." The next day, Thursday, the Oil Company informed Vincent that they had advanced the price of the property. It was held that Vincent's statement that he considered the trade closed was not an absolute acceptance, but merely the expression of his opinion that the purchaser whom he had in tow would in all probability accept the property. The Oil Company's withdrawal of the first offer was made in proper time, when they notified Vincent of the advance in price.

Rule 12.—After acceptance the offer is irrevocable, and neither party may change any of the terms of the contract without the other's consent.

The contract springs into being at the moment the acceptance of the offeree unites with the offer. The two parties are thereupon bound together. The legal ties which connect them in the contractual relation would not be worth anything if either party could drop the contract at his pleasure, without incurring any responsibility. Even though the performance of the contract is set for the future, it binds the parties as soon as it is made. Neither party can lawfully dissolve it without the other's consent, merely by notifying the other party of his intention not to live up to it.

Since the contract is binding when first formed, it follows that neither party may change a single term of it against the other's wish. If one party could partially defeat the contract by altering any term of it, he might as well be given the power of destroying it altogether.

The case of *Campbell v. City of Philadelphia* (1881), 10 W. N. C. 221, brings out this principle. The Philadelphia Board of Health had advertised for bids for cleaning certain streets. The terms were set forth in the advertisement, and one of them provided that the successful bidder must give certain security. The contract was awarded to Campbell, and he was ready to furnish the security mentioned in the advertisement, but the agreement which he was asked to sign contained a clause for holding back half of certain monthly payments for almost a year in order to give the city better security. Campbell objected that the terms of the contract which had been made with him provided for regular monthly payments, and that the clause for holding back half of several monthly payments was a new term to which he had never assented. Campbell refused to sign the agreement presented to him, and obtained an injunction prohibiting the city from advertising again for other bids. This case, while it serves to illustrate Rule 12, would be decided differently if it arose to-day, because the new Philadelphia charter requires city contracts to be in writing. *Smart v. Philadelphia* (1903), 205 Pa. 329.

When a dispute centers on the question as to whether or not a certain term was part of a contract, it is not always enough for the man who objects to the term to prove that he did not know about it at the time. If he has signed a written agreement in which the term is to be found, the mere fact that he hurriedly glanced over the agreement without noticing the term will not excuse him. He is presumed to act the part of an ordinarily reasonable man, and he cannot escape liability if he closes his eyes to the existence of a term in the agreement which he signed. This principle rules many cases where a bill of lading or a ticket is accepted by a man who is paying for the transportation of his property or of himself. When a railroad company issues a bill of lading, that usually

constitutes the contract between the parties, even though the shipper of the goods does not sign it. The terms and conditions which are legibly printed on the bill of lading may fairly be said to be incorporated into the agreement of transportation. If, however, they are printed in extremely small type in a corner of the bill of lading to which the shipper's attention would not likely be directed, it could be properly argued that they should not be considered part of the contract. A similar distinction may be drawn with respect to a notice posted in the office of the railroad company. If this notice contains the terms and conditions upon which goods will be received for shipment, and if it is printed in flaming red letters, and is placed where it should catch the eye of every person entering the office, the terms and conditions which it sets forth are to be considered part of the contract, where there is no written or printed contract, even though the shipper through his own heedlessness fails to note them. If the notice is printed in small type, or posted in an obscure part of the office, it plays no part in the contract, unless as a matter of fact the shipper happened to see it.

CHAPTER III.

THE SECOND ELEMENT NECESSARY IN ALL CONTRACTS, SEAL OR CONSIDERATION.

Not every promise is enforceable at law. It may have been very clearly made in writing and by a person of sound mind. There may be no suggestion of fraud or the least impropriety about it. Nevertheless, if the second element, seal or consideration, is lacking, the promise is not enforceable. There is no contract. The first element is called offer and acceptance, because the meeting of the minds of the contracting parties requires both an offer and an acceptance. The second element is called seal or consideration. The word "or"

indicates that both seal and consideration are not necessary in a single contract; one is usually sufficient by itself without the other.

(A) SEAL.

Let us first understand what is meant by a seal. Formerly it consisted of an impression stamped on a lump of wax. The wax was attached to the written document which set forth the agreement. The presence of the seal was regarded as proving that the agreement was solemnly made, and was seriously intended to bind the parties firmly. In ancient times courts were few, and it was not believed that governmental enforcement of private agreements was an important function of the organized civil power called the State. Many ancient governments undertook, however, to enforce certain private agreements which were entered into with due formality. The seal is a survival of the ceremony with which it was formerly necessary to make a binding contract.

At the present day some seals are stamped on wax in accordance with the old custom. The trouble incident to the use of a wax seal has led to the adoption of a simpler form of seal by most people. Many years ago men began to reach the conclusion that a gummed disc of colored paper, which could be easily fastened to a document, would accomplish the same purpose as a wax seal, because it would indicate that the parties to a written agreement desired to give the agreement the appearance of having been made with solemnity. The intention of the parties to dignify their written agreement by putting a seal on it is the thing which the courts are mainly concerned about, and this intention could be gathered from the presence of a paper wafer pasted upon the document, as well as from a wax seal tied to it with a ribbon. After the introduction of the paper wafer as a substitute for the wax, somebody hit upon the idea of preparing printed forms of contract with the likeness of a seal printed near that part of the paper where the signatures of the parties would be made. This innovation gained popular approval, for it saved the time and trouble of

attaching anything to the document, while it indicated the intention of the parties to treat the document as sealed. Ordinarily, therefore, where the parties to an agreement fill in and sign a printed form of contract, and write their signatures to the left of the printed imitations of seals which are already on the paper, they are supposed to adopt the printed seals. The instrument, therefore, is called a sealed instrument, and the solemnity and binding character of the printed seals will be just as great as if wax seals had been attached by the parties to the paper which they signed.

The intention of the parties to make their agreement a sealed contract governs the courts, but if the parties actually fail to have any kind of seal whatever, the document is not regarded as being sealed, even though it may recite that they have signed and sealed it. Almost any mark, however, which the parties may intend as a seal will legally take the place of the old-fashioned wax seal. For instance, a rude scroll made with the pen after the signature of each party will be considered as the equivalent of a more pretentious seal. Sometimes the mere word "seal" or the letters "L.S." will be used as a substitute for the wax. These letters are the initials of the Latin words "*locus sigilli*," meaning "the place of the seal." Again, a circle or even a hasty scratch of the pen, if intended to represent a seal, will be treated by the courts as a legal seal. Prudence, however, suggests that some care be taken to avoid the possibility of misunderstanding. Where the document is to be sealed, it involves no great trouble to fasten red paper wafers on the right hand side of the place allotted to the signatures of the parties. It is customary to have a separate seal for each of the contracting parties. The seals are usually prepared at the time the instrument is drawn up, and each party afterwards signs his name to the left of one of them when the instrument is executed. The signature alongside of the seal betokens that the party who made it adopted the seal as his own.

There is danger if one carelessly makes a rough scrawl with a pen to represent a seal, that it may afterwards be mistaken for a mere flourish which many persons append to their signatures. In order to avoid doubt as to the intention to

represent a seal, and to prevent the scrawl from being regarded as only a blot or a flourish of the pen, it is usual to recite in the body of the agreement that the instrument is sealed. Suppose, for instance, that a man desires to bind himself to give Daniel Leno, any relative or acquaintance, one hundred dollars. Suppose he is under no legal obligation to pay the money, but desires to create a legal obligation by using a seal. He could properly accomplish his purpose by signing his name at the foot, of the following form of agreement where the word "signature" is inserted:

September 1, 1906.

*One day after date I promise to pay to Daniel Leno
One Hundred Dollars.*

*In witness and confirmation whereof I have here-
unto set my hand and seal.*

(Signature.) (Seal.)

If the reader wants to follow this subject further, he should look up for himself the case of *Lorah v. Nissley* (1893), 156 Pa. 329.

Suppose John Smith promises a friend, Peter Jones, to give him \$50. If the promise is merely made out of friendship, it is not enforceable at law, whether made by word of mouth or in writing. Suppose, however, that John Smith signs the following memorandum, and writes the word "seal" after his name: "On demand I promise to pay Peter Jones \$50." The presence of the seal gives Peter Jones the right to ask aid of the courts in forcing Smith to keep his promise. Why should the courts attach so much importance to the word "seal"? Because for centuries it has been the custom to regard a promise under seal as solemnly binding, and John Smith has clearly brought himself within the operation of that custom. We shall see something more about seals further along in this chapter, but for the present we shall take up the subject of consideration.

(B) CONSIDERATION.

Consideration may be called a substitute for a seal. As a general rule, it may be stated that the second element necessary in every contract consists of either a seal or consideration. Sometimes both a seal and consideration are found in the same contract.

Originally the formality of a seal was usually thought to be the one essential thing which made a promise enforceable at law. As trade increased it was found desirable for the State to promote credit and prevent bloodshed by enforcing certain agreements even though not made under seal. If a man borrowed money from another, and refused to repay it, the law would lend its aid to the creditor, for the loan of the money came to be regarded as supporting and making legally enforceable the debtor's promise to pay it back. The benefit received by the debtor in exchange for his promise to pay the money was called the consideration which would move the courts to enforce the debtor's promise against him, irrespectively of a seal. Again, if a man received goods which he had bought from another, the sale and delivery of the goods to him was deemed to be a consideration making his unsealed promise to pay for them enforceable. Gradually the doctrine of consideration grew, until now if a promise is given in exchange for anything of value, the promise will be enforceable, provided that it relates to such matters as come within the scope of the courts' jurisdiction. *Consideration, therefore, is something which is exchanged for a promise.*

In a former part of this chapter it was stated that if John Smith makes a promise out of mere friendship to pay Peter Jones \$50, the promise is not enforceable unless made under seal. Suppose now that there is no seal, but that Jones hands Smith a certain book, and that it is agreed between the parties that Smith shall pay Jones \$50 for that book. Smith's promise is enforceable, because Jones sold and delivered the book to him in consideration of Smith's promise to pay the money. In the case we are studying there is no seal, but the delivery of the book constitutes consideration, which is a substitute for a seal.

There is an exchange of values between the parties, and it is only fair that Smith, having received the book, should be compelled to pay the money which he agreed to exchange for it. The two things, the book and the money, balance each other in the scales of justice. The parties have made an agreement by which each was to get something. The delivery of the book by Jones was made in consideration of Smith's promise to pay the money, and Smith's promise to pay the money was given in consideration of the delivery of the book. So far as the second element, seal or consideration, is concerned, by far the greater number of contracts depend for their validity upon consideration. The following are some rules on this topic:

Rule 1.—Consideration may consist either of some advantage gained by the maker of the promise or of some disadvantage suffered by the party to whom the promise is made.

This rule is sometimes expressed as follows: Any benefit to the promisor or any detriment to the promisee may be sufficient legal consideration. We are now studying the enforceability of promises. It will save time to call the party who makes a promise "the promisor," and to call the party to whom the promise is made "the promisee." In most contracts each party promises something to the other. Each party will, therefore, be a promisor as respects the promise which he gives to the other. Each party will also be a promisee as respects the promise which is given to him. In analyzing the formation of a contract, the words "promisor" and "promisee" are used (just as the words "offeror" and "offeree" are used) in examining the way in which the minds of the parties come together. The words "promisor" and "promisee" must be employed with reference to a certain definite promise.

The first part of our rule states that any advantage to the promisor may constitute consideration. If you promise a man ten dollars for cleaning your room, or repairing your automobile, or obtaining a book for you, and the man does what he agreed to do, he may secure the aid of the courts in forcing you to pay him the ten dollars. Any service for which you agreed

When a promise is given for a promise, each forming the consideration for the other, such consideration is said to be executory or future. Where an act is given for a promise the consideration is said to be present.

to pay the money is regarded as being of some benefit to you, and will be consideration to support your promise. If you have agreed to pay ten dollars for any article of property, the party with whom you made the agreement may, upon delivering the property to you, force you to pay the money. You have received consideration for the making of your promise, and you can be obliged to fulfil it.

The second part of our rule states that *any disadvantage* suffered by the promisee may constitute consideration. Suppose that a creditor is pressing his debtor for payment, and is about to have the sheriff sell the debtor's property. Suppose that a friend of the debtor agrees to pay the creditor \$30 if the creditor will delay his legal proceedings for a month. If the creditor enters into this agreement, and keeps his part of it by holding the sheriff back for a month, he may compel the debtor's friend to pay him \$30. The debtor's friend may object that he personally received no benefit from the delay. It is true that he got nothing for the giving of the promise, so that no benefit was received by the promisor in exchange for his promise to pay \$30. The consideration consisted in the disadvantage suffered by the creditor, the promisee, who delayed his suit a month in return for the promise which was made to him. He suffered a certain detriment by binding himself to hold off for that period of time, and this detriment is sufficient consideration to support the promise of the debtor's friend.

Again, suppose a merchant applies to an insurance company for a policy of fire insurance, and the policy is issued for six months, and remains in force during that time. Suppose that the merchant has not paid any premium during the life of the policy, and is sued after it expires for the unpaid insurance bill. He may, perhaps, defend on the ground that his promise to pay the premium was not supported by any consideration, and he may prove that the insurance company was not called upon to make good any loss, assuming that the merchant has not suffered from fire during the term of the policy. The insurance company's answer to this would be that they incurred a certain risk and responsibility when they wrote the policy. This was a detriment to them, and would constitute consideration to make the merchant's promise enforceable.

Rule 2.—The mere fact that the advantage to the promisor or the disadvantage to the promisee is very slight will not prevent its being consideration.

Where parties make a bargain, each is supposed to look out for himself. After the agreement is made neither party should try to back out of it. If the judges find that one party wants to break his promise merely because he is dissatisfied with the terms of the contract, they will give him no relief. The courts do not sit for the purpose of telling citizens what kind of bargains they should make. Citizens are supposed to make their own contracts, and the business of the courts is largely to see that the party who breaks his contract shall pay damages to the injured party.

The second rule, therefore, forbids one, who has received consideration for a promise, to refuse afterwards to fulfil the promise on the mere ground that the consideration was very meagre and inadequate to the promise. The courts will not undertake to say that the consideration was not sufficient, for the party who made the promise agreed himself to take the consideration in exchange for it. This rule was applied in the case of *Potter v. Hartnett* (1892), 148 Pa. 15. Potter sued Hartnett to realize the amount of a judgment which he had recovered against Hartnett in New York sixteen years previously. Hartnett's defense was that, after Potter's claim had arisen, Potter had been engaged by Hartnett's firm upon the agreement that their employment of him was to be accepted as full payment of the claim. To this Potter objected that the mere agreement of Hartnett's firm to employ him could not be sufficient consideration for his promise to abandon his claim, because he rendered valuable services while employed by Hartnett's firm. He contended that the wages paid to him by Hartnett's firm were merely consideration for his work on behalf of the firm. The Supreme Court, however, held that if he had agreed to drop his claim in return for the firm's acceptance of him as an employee, it was sufficient consideration to make his promise to drop the claim legally binding on him.

In the case of *Potter v. Hartnett* the agreement of Hartnett's firm to pay Potter wages served as consideration to balance Potter's agreement to do two different things, first, to work for the firm, and, second, to drop his claim. Sometimes a man may promise to do a dozen different things if another man will do a single thing for him. If it is clearly understood that the man who is to do twelve things must do them all in return for the one thing which the other party is to do, the single action of the latter will serve as consideration for each of the twelve actions of the former. For instance, if it is agreed that A shall pay B \$50, for which B is to give A a certain machine and is also to go on a certain journey for A, B's two promises are supported by A's payment of \$50. It will not do for B to say that one consideration cannot support two promises, because the two promises were made by him in exchange for the single consideration, and he gets what he bargained for.

If a man agrees to sell property which is worth a thousand dollars for twenty dollars, the agreement is just as binding on him as if he were to get the full value of what he sells. The size of the consideration makes no difference, so far as concerns the necessity of having the second element, seal or consideration, present in every contract. Inadequacy of consideration, however, may sometimes be regarded as one circumstance going to show that a contract was fraudulently made. Combined with other indications of trickery, the fact that a very small consideration was given for a certain promise may be of use in defeating a contract on the ground of fraud.

The detriment to the promisee which may constitute consideration to support the promise need not be very serious. If the party to whom a promise is made suffers any risk or delay or inconvenience in return for the giving of the promise, he can enforce the promise just as well as if the consideration for it were quite valuable. Consider again the case of the creditor who delays action against his debtor at the instance of the latter's friend. The debtor's friend agrees to pay him \$30 for one month's forbearance. Suppose the creditor keeps his agreement, and sues for the sum of \$30. The debtor's friend who promised to pay this sum may, perhaps,

defend on the ground that the creditor suffered no real harm by the delay. The courts will not permit him to make any capital out of this fact, for if the creditor has done his part by surrendering his right to proceed against the debtor for a month, then the debtor's friend must also do as he agreed. The creditor forbore to exercise a legal right, the right of pressing forward his suit, and this detriment to the promisee is enough to make the friend's promise to pay the sum of \$30 enforceable.

In order to sustain *subscriptions to charities*, the courts have shown themselves particularly anxious to discover some consideration which will make the promise to contribute binding. In the case of *Presbyterian Board of Foreign Missions v. Smith* (1904), 209 Pa. 361, Smith was the executor of a decedent named Waters. Waters had promised to pay \$10,000 to the Mission Board as a memorial to his mother, for use in the Chinese mission work. A witness testified that when Waters spoke of establishing this memorial, the witness went to New York, and obtained the Mission Board's agreement to accept the money for the purpose desired. This was reported to Waters, who paid \$2,000 out of the \$10,000, and promised to pay the rest in four annual instalments. Accordingly, two missionaries were appointed, and sent to the Chinese province of Hunan, and by reason of Waters' promise the Mission Board refrained from trying to raise funds elsewhere to maintain their missionary work in Hunan. Waters died, and his executor declined to carry out the promise on the ground that it was not based upon consideration. The Supreme Court enforced the promise to pay the balance of \$8,000, holding that the obligation assumed to do the work for the purpose contemplated, the entering upon the performance of an integral part of the work, the refraining from making collections from other persons and the employment of missionaries, all established a sufficient consideration for the obligation assumed by Waters. Indeed, the court intimated that the mere acceptance by the Mission Board of Waters' promise, and their agreement to devote the money to the purpose he desired would have been sufficient consideration to make his promise binding, in case he had died before paying anything, and before the missionary

work had been set on foot. This case shows that where the consideration consists of a detriment to the promisee, the detriment may be slight, without impairing the legality of the consideration, especially in the case of a promise to contribute to a charity.

Rule 3.—A promise by one of the parties is sufficient consideration for a promise by the other party.

If a bookseller sells and delivers a book to a customer, he has given consideration which will make the customer's promise to pay the price of the book enforceable. Suppose, however, that the bookseller has not yet published the book, but the customer knows what it will be like, and promises to pay a certain sum for a copy of it when published. May the bookseller after the book comes out compel the customer to pay for it? The customer may object that he received no consideration for his promise to pay for the book. If the bookseller did not promise to sell the book to the customer, and the customer withdrew his promise before the bookseller accepted the order or took any step towards filling it, the customer's contention would be correct. If, on the contrary, the bookseller accepted the customer's order, and promised to fill it, there would be a binding contract between the parties, and the customer's promise to pay for the book would be enforceable at law. The consideration for this promise would be the corresponding promise of the bookseller to sell the book. It would not be necessary for either party to pay anything to the other to bind the bargain. Their mutual binding promises are sufficient. The obligation which the bookseller undertakes of delivering the book balances the customer's obligation of paying for it. In other words, the right which the customer acquires to hold the bookseller to delivery is consideration for the right which the bookseller acquires to hold the customer to payment.

If the two promises are to be fulfilled at the same time, one party cannot make the other live up to the contract, unless he is ready and willing to perform his own part of it. Suppose, on the other hand, that the two promises are to be fulfilled at different times. When the time for making good one

promise arrives, suppose that the party who gave it fails to keep it. The injured party may bring suit at once, though the time for performing his side of the contract has not arrived. His promise which has not yet matured is consideration to make enforceable the promise of the other party which has matured.

Rule 4.—The compromise and settlement in good faith of a disputed claim constitute consideration to support the terms of the compromise and settlement.

Courts favor the private adjustment of disputed matters, when it is made in good faith. The terms of adjustment may embrace certain things which are to be done by each party. Each party promises to do certain things, and his promise is enforceable, since it is made in consideration of the settlement of a dispute. For instance, where parties have been in a number of complicated transactions, and the accounts between them are in a tangle, they may conclude to settle all matters by having one person pay the other a certain lump sum in cash, without unraveling all the difficulties which their accounts present. If they choose to make such a contract, the man who was to pay the cash to the other cannot afterwards object that a full accounting should be made, and that experts should be employed to discover how their affairs really stand. He has freely consented to dispense with the ordinary accounting, and has entered into a binding compromise. His promise to pay a certain sum to the other party is, therefore, enforceable against him.

Frequently claims for personal injuries are presented to railroad corporations and other companies. The companies investigate these claims, and usually arrange to settle them if the claimants have good cases. If, for instance, a railroad company has agreed to pay a passenger who was injured in a collision the sum of \$200, and the passenger has agreed to accept that amount in settlement, there is a binding contract between the parties. If the injuries afterwards rapidly disappear, the railroad company is not free to repudiate its agreement. On the other hand, if the injuries subsequently turn out to be very serious, the claimant must abide by the terms

of the settlement. If, however, it subsequently comes to light that one of the parties procured the settlement by fraud, the other party may repudiate it, but questions of fraud are not to be studied until we come to the fifth chapter.

—4 The case of *Fink v. Farmers' Bank* (1896), 178 Pa. 154, illustrates the fourth rule. Fink was surety on the bond of a bank cashier, who embezzled some of the bank's money. Fink was asked to make the loss good, and gave his notes for the amount which had been embezzled. Afterwards he sued the bank for the return of the notes, alleging that the surety bond signed by him had expired before the date of the embezzlement. The court refused to set aside the private adjustment of the dispute which Fink had made with the bank. There was no concealment, imposition or other element of fraud in it. The surety bond had been surrendered to him in exchange for his notes, and the court declared that the sufficiency of the consideration for a compromise is not to be determined by the soundness of the original claim of either party. The very object of compromise is to avoid the risk or trouble of determining the question of the soundness of that original claim. The bank had an immediate right of action on the bond, and Fink after making the compromise was no longer free to assert that an action on the bond would surely have been decided in his own favor. He had gained an extension of time for the payment of the claim when the bank received his notes in settlement. Rash persons sometimes hastily agree to a compromise, and afterwards regret what they have done, and try to back out of it. The courts have no sympathy with them, for they are supposed to mean what they say when they agree to the terms of settlement.

Rule 5.—The doing of what one is already legally bound to do is no consideration.

From the fourth rule we know that if a creditor claims a certain sum from his debtor, and there is an honest difference of opinion between them as to the amount due, a compromise whereby the creditor agrees to accept less than he claimed in full settlement will be binding upon him. Under the fifth rule let us picture another situation. Suppose that there is no dis-

pute as to the amount of the debt, which is agreed to be \$1,000. Suppose that the creditor promises the debtor to forgive the debtor half of this amount, if the debtor will pay him \$500. The debtor manages to raise \$500, and pays it over. The creditor has a perfect legal right to sue the debtor for the remaining half of the debt. He promised to forgive the debtor \$500 of the debt, if the debtor would pay him the other \$500, but there was no consideration to make the creditor's promise enforceable. There was no benefit to the promisor, for the promisor, the creditor, when he received \$500 from the debtor was merely getting that to which he was already legally entitled. There was no detriment to the promisee, the debtor, and he suffered no loss or disadvantage in return for the giving of the promise. The debtor might argue that he would never have paid the sum of \$500, if the creditor had not agreed to forgive him the balance of the debt, but when he says this he declares that he would have shirked a legal obligation to pay the whole debt but for the creditor's promise to let him off on payment of half of it. The debtor did not give anything up in exchange for the promise save what he was bound to surrender to the creditor whether or not the promise had been made. The situation is the same as if one man were to promise to give another \$500. If the promise is not made under seal or supported by a consideration it cannot be enforced at law.

Suppose that a debtor who wants to be legally released from a thousand dollar debt hits upon the device of agreeing with his creditor to pay \$500 and a hat or a book. If the creditor promises to release the debtor entirely in consideration of the money plus the hat or the book, the creditor's promise to drop his claim to the other \$500 would be binding. From Rule 2 we know that the smallness of consideration does not affect its legality. A hat, therefore, or a book, or a cane or any other article would be sufficient consideration to support the release of the debtor. The situation would be the same as if a man were to agree seriously to pay \$500 for a certain book or cap or cane. He would be bound by the agreement, and could not object to the inadequacy of the consideration.

These principles are of great practical interest in financial adjustments, which are sometimes made when a merchant

becomes insolvent, and tries to arrange with his creditors so that he will be allowed to continue his business. If the debtor can raise enough cash to pay each creditor 60 per cent, he will probably want to be released from all obligation to pay the remaining 40 per cent of his debts. If each creditor were to agree separately, and without regard to the action of any other creditor, to accept 60 per cent and forgive the remainder of his claim, the promises of the separate creditors would not be binding on them. Sometimes the debtor under these circumstances will get his creditors to give him a release under seal for the balance of their respective claims. More frequently, however, the object in view is accomplished by having the creditors who are willing to compromise unite in a *composition agreement*. This agreement is usually put in writing in order that the debtor may preserve evidence of it. It sets forth that the creditors who join in the compromise agree with the debtor and with each other that each creditor shall accept a certain percentage of his respective claim in full payment thereof. The fact that more than one creditor joins in the composition introduces the element of consideration, which makes enforceable the promise of every creditor who takes part in it to forgive the unpaid remainder of his claim. What is this consideration? It consists of the mutual forbearance on the part of the creditors who join in the composition. There is a "give and take" in it, which is at the bottom of the idea of consideration. Each creditor who enters into the composition agrees to accept a portion of the money due him in full settlement, upon the consideration that the other assenting creditors will do likewise. Each assenting creditor understands that if he were to bring suit, other creditors might take the same step, and the result might be a disastrous failure with dismal prospects for everybody. He agrees, therefore, to be contented with a certain percentage of his claim, in consideration of the making of a similar agreement by the other creditors.

It is not necessary that the majority of the creditors of any debtor should join in a composition agreement, for even if only two creditors agree with each other to take less than the full amount of their claims, the agreement will be binding. In actual practice, however, it is found that most creditors are

unwilling to take part in a composition, unless all or at least a majority of the other creditors will likewise fall in line. Where the terms of the composition agreement provide that it shall not take effect until assented to by all the creditors, no single creditor is bound until the condition that the consent of all is to be secured has been fulfilled. It is far better not to provide that all the creditors must join, for then a single creditor can defeat the entire composition by refusing his consent. Ordinarily, composition agreements require merely a majority of the creditors to join before they will take effect. Sometimes they are silent on the subject of the number who must join, and in this case they bind those who give their assent whether a minority or a majority.

A composition agreement is a contract which binds those who make it. Those who refuse to have anything to do with it are usually not affected by it. In the fourth part of this book, however, we shall see, under section 12 of the Bankrupt Act, that after a debtor has gone into bankruptcy a composition agreement which binds all his creditors can be put through with the consent of a majority in number and interest.

Very often a debtor, who is endeavoring to get his creditors to sign a composition agreement, will offer a secret inducement to some of the bigger creditors. In order that they may help sway the others he will privately promise them a larger percentage than the others are to get. The creditors who lend themselves to this disgraceful scheme help to perpetrate a fraud upon the other creditors. Needless to say, they cannot sue the debtor afterwards upon his agreement to pay them the balance of their claims, for the courts will not lend themselves to aid this fraud. On the contrary, the courts will permit any of the deceived creditors who have been lured into signing the composition on false representations, to repudiate it, and recover the balance of their claims.

X Returning to our fifth rule, we find an illustration of the way it works in the case of *Smith v. Whildin* (1848), 10 Pa. 39. A constable had been handed a warrant for the arrest of a man named Crossin. The prosecutor promised him a reward of \$100 if he would make the arrest, which he succeeded in doing. He sued to enforce this promise, and the defense was that no

consideration had been given for it. The court sustained the defense, declaring that a constable is required by law to do his utmost to arrest offenders when a warrant for them is put into his hands. If the prosecutor had chosen to keep his promise, it would be all right for him to pay the reward, but his promise was not binding on him, for it was unsupported by consideration. The law provides what fees are to be paid to constables, and the reward in question was to be given as an additional perquisite to the constable who brought this suit. If he had been specially employed to do something outside of his official duties (as, for instance, to procure evidence), he should be allowed to demand payment for his services in such unofficial matters. As an officer of the law, however, he must not stipulate for special fees for doing what he is bound to do faithfully for the ordinary fee prescribed by law.

The same principle was applied in a suit brought by a sailor to recover additional compensation. He had been employed for a certain voyage, and during the course of the voyage the ship was in danger of being lost. The captain promised this sailor to pay him extra for helping to work the ship. The promise was not binding, because no consideration was given in exchange for it. The sailor was bound under the contract which he made when he went aboard the ship to do his utmost for her safety. The captain's subsequent promise was given, therefore, only as an inducement for the sailor to do what he was already bound to do, independently of any fresh agreement. It seems only fair that the sailor should have received no encouragement in his effort to take undue advantage of the danger in which the ship was placed by obtaining a promise to pay additional compensation for his services.

Rule 6.—A subscription to a charity, or to stock in a proposed corporation which is not yet formed, is supported by consideration if the subscription of the promisor in question helps induce others to subscribe.

It was explained under Rule 5 that where several creditors of the same debtor agree together to accept a portion of their respective claims in full settlement, they are bound by their

promise. A creditor making such a promise (unsealed) without respect to similar action by other creditors is not bound thereby, for in that case the promise is not supported by consideration. Where several creditors join in a composition agreement, their mutual promises constitute consideration. One enters into the composition by reason of the fact that the others agree to do so, and thus all who join are bound by its terms.

A like situation exists where a number of persons subscribe together to a charity. One's promise is partly induced by the fact that others have done or are going to do the same thing. The promises, therefore, depend on each other, and each one is enforceable, since the other promises were to some extent induced by it. When, therefore, a person subscribes towards raising a fund for a charity, he cannot legally release himself from liability by giving notice that he has changed his mind, if it appears that other persons have been induced to contribute, or to agree to do so, on the faith of his promised contribution.

Again, where a number of persons plan to get up a corporation, and a subscription list is sent around, the various subscribers who agree to take stock are bound to do so when the corporation is formed. The basis of this liability seems to be two-fold: first, each subscriber, except the last, has presumably helped to induce others to subscribe; second, the expenses and trouble of forming the company have been incurred on the faith of the subscriptions. The latter is probably the stronger reason, for in the case of subscriptions to take stock in a corporation not yet formed, any subscriber is allowed to cancel his subscription, unless he delays until the incorporation actually takes place. Apparently the courts are quicker to uphold a subscription to a charity than to a corporation, for a subscriber to a charity cannot withdraw if subsequent subscriptions have been induced by his own. Furthermore, a promise to contribute to a charity need not be in writing, while a promise to take stock in a corporation not yet chartered is not binding if made merely by word of mouth. Promoters of corporations should, therefore, insist on having subscribers sign their names to an agreement clearly and fully stating their obli-

gation to buy a certain amount of stock when issued by the future corporation. It is not absolutely necessary for a subscriber to sign his own name. If another signs it for him at his direction, the agreement is enforceable against him.

Rule 7.—Before a contract has been performed, the parties may by a second contract change the terms of the first one, and their mutual promises will be sufficient consideration for the new agreement.

If A and B make a contract whereby each promises to do something for the other, A's promise will be consideration to make B's promise binding, and similarly A's promise will be enforceable because supported by the consideration of B's promise. If A completes what he is to do, but B has not done his part, and A agrees to release B from B's obligation under the contract, A's promise to forgive B is not binding, because he has received no consideration for it. An example of this is found in the case of a creditor's agreeing out of kindness for a debtor to forgive the latter's debt. The creditor may turn around the following day and bring suit for the money, because his promise to drop the matter was unsupported by consideration. Suppose, however, that neither A nor B has completed his work under the contract, and they agree that both shall stop work, and drop the contract entirely. They are free to annul the contract, just as they were free to make it, and the promise of each of them to release the other is supported by consideration. They mutually forgive each other. A releases his right against B. B releases his right against A. The obligations which each owed the other are mutually cancelled.

Applying what has just been said to the seventh rule, let us imagine that A and B, instead of abandoning the old contract entirely, and ceasing to do business with each other, merely want to substitute a new contract in place of the old. The old contract has not been fully performed by either, but they are at liberty to cancel it, and the new contract will take the place of the old one. The new contract is called a novation.

The case of *Dreifus, Block & Co. v. Salvage Co.* (1900), 194 Pa. 475, furnishes an example of a novation. In February, 1895, the Salvage Company agreed to sell Dreifus, Block

& Co. three thousand tons of the steel framework which the Salvage Company was removing from the World's Fair buildings in Chicago. The Salvage Company was to shear the heavy framework into lengths of six feet, so that it would be more suitable for remelting. The Salvage Company's shearing machine broke down, after some of the steel had been delivered, and in September, 1895, the parties agreed to cancel the existing contract. Dreifus, Block & Co. promised to accept two hundred tons sheared into six-foot lengths and nine hundred tons of unsheared steel framework. It was agreed that they should pay the same price for the unsheared steel as had been fixed by the February contract for the sheared steel. The terms relating to delivery and dates of payment were the same in the September contract as in the February one. Afterwards Dreifus, Block & Co. tried to set aside the September contract, and to revive the more favorable February one, for the sheared steel was worth more than the unsheared. The court decided that they could not do this, because they had agreed to cancel the February contract, and to replace it with the September one.

Sometimes it is hard to say whether there is a novation or merely an unenforceable promise subsequently made by one party to release the other from a contractual obligation. In the case just mentioned the parties clearly agreed to cancel the first contract. If there had been no such agreement, but a bare promise by Dreifus, Block & Co. to release the Salvage Company from the obligation of shearing the steel, this promise might have been withdrawn by Dreifus, Block & Co. It would have been merely a naked promise to release the Salvage Company from an obligation imposed on them by the old contract, and as the old contract would still continue in force, uncanceled, it would still bind the Salvage Company to shear the steel into six-foot lengths, at the demand of Dreifus, Block & Co.

The case of *Cannon v. Young* (1896), 5 D. R. 772, exemplifies this last idea. Cannon delivered 500 cases of corn to Young, who gave him a note for the price. When Young was sued for the money he declared that Cannon had afterwards

promised to let him pay from time to time as he should be able to dispose of the corn. In other words, Young rested his defense on a subsequent promise to forgive him from the legal obligation of paying at the maturity of the note, and to extend the time of payment for each case of corn until that particular case should be disposed of by Young. The court held that the promise to give Young more time was based on no consideration. Cannon had done his part, and Young was under an obligation to pay the note when it fell due, from which he could not be released by Cannon's bare promise to grant him more time. There was not any novation in the case of *Cannon v. Young*. We shall glance again at this topic in the fourth part of the present book, under the heading "Discharge of Contract by Agreement."

Rule 8.—Consideration may be present or future, but a past consideration is not sufficient to support a subsequent promise, except in certain special cases.

If A agrees to do a certain service for B in return for the payment of five dollars, and B hands him the money at once, A's promise is supported by a present consideration. If the money is to be paid to A on the completion of his work, his promise is supported by a future consideration. In the latter case, we have an illustration of the third rule, for it is B's promise to pay A the money that makes A's promise to do the work enforceable. Coming to our eighth rule, let us suppose that A has at some time in the past, a year or a month or a day before promising to work for B, received the sum of five dollars from B by way of a gift. A is grateful to B and promises B to perform the work in question. He is not bound to do the work, because he received no consideration in exchange for his promise. B's previous gift supplied the motive which prompted A to give the promise, but a mere motive is no legal consideration. The consideration must be given in return for the promise, and it cannot be argued that B's previous gift was made in consideration of a promise which was subsequently given. The essence of consideration is that it shall be given in return for the promise. It must be given on

account of the promise, and must be traded for it. The two must be intended to balance each other. The past gift which was made to A had already been received by him. It belongs to him anyway, and can be enjoyed by him whether or not he makes the promise.

We should try to grasp the theory of consideration. Suppose two friends, X and Y, are talking together. In the course of their conversation X promises to give Y a painting which Y admires. Their talk drifts to other subjects, and X mentions that he needs a trusty messenger to take a valuable package to New York for him on the following day. Y promises to carry the package for X. If Y breaks his word and tells X a few minutes later that he has changed his mind, and that he will not go to New York, X has no legal claim against him. X promised to give Y the painting, but the two promises were not exchanged for one another. They have no relation with each other, since one promise was not agreed to be given in consideration for the giving of the other promise. The promise to give Y the painting was made before the giving of Y's promise, and the two were not connected by any legal agreement. Perhaps Y was urged to make his promise by the feeling that X had been kind to him, and that he ought to do something for X, but this does not constitute the kind of bargain in which the courts can see that the two promises were agreed to be balanced against each other and to depend entirely on one another.

It should be mentioned that if Y had received the package, and had lost it through gross negligence while taking it to New York, he would be liable to X. His liability would not be based on a contract between him and X, but merely on his negligence in performing a task gratuitously assumed. Take a parallel case. Suppose Y promises a friend that he will ride the latter's horse to New York, where the friend wants to stable it. If Y has agreed to perform this service merely out of friendship, and is not to get paid for it, he is legally free to break his word, and refuse to ride the horse to New York. If he starts out with the horse, however, and recklessly jumps fences with it, in order to amuse himself, thereby injuring the

horse, he is liable to his friend for the damages occasioned through his negligence. This liability is not contractual, but is based on the wrongful injury to another's property, respecting which he was bound to take some care.

There are a few cases in which promises have been held enforceable although founded on a past consideration. These are cases in which the courts have regarded the position of the promisee as specially meritorious, and as justifying a departure from the general rule. The first class of decisions in which this exception appears presents the situation of a debtor who promises to pay his creditor money which he previously owed, but which he is not legally bound to pay. The debtor has never satisfied his obligation to pay the money by giving it to the creditor, but the creditor's right to enforce payment has been legally barred. The courts recognize that the moral obligation to pay the money still remains, even though the right to enforce the former legal obligation has been lost to the creditor. It must not be imagined that whenever a moral obligation exists there is a corresponding legal obligation which the courts will enforce, but in the cases to be mentioned the courts are so impressed with the strength of the moral obligation that they go out of their way to uphold it with the sanction of civil law.

Where a debtor has not promised to pay a debt for six years after it has become due, or given any such acknowledgment of it as indicates a promise to pay it, a statute provides that the debt is unenforceable, unless the creditor has begun suit before the expiration of the six years period. If, however, the creditor has obtained a new promise to pay the debt, it is enforceable for another six years; and if he has obtained judgment against the debtor, or has received a promise to pay the money made by the debtor under seal, the debt is not outlawed for twenty years. *Where the enforcement of the creditor's rights is barred by the lapse of time, a subsequent verbal or written promise by the debtor will revive the claim.* No new consideration need be given for this purpose, because the past consideration will be enough. This past consideration usually consists of the loan of money or the sale of goods. The old obligation, formerly resting on the debtor but since outlawed, is re-

garded by the courts as sufficient to support the debtor's subsequent promise to pay the debt. If the subsequent promise is made verbally or by an unsealed writing, the creditor has six years from the date when the new promise is given within which he may bring suit to enforce it. If the subsequent promise is made under seal, the creditor may bring suit within twenty years from the date of the new promise.

A creditor to whom a large amount has been due for several years should beware of letting his claim become outlawed. If he starts suit within six years from the time when the debt arose, and finally recovers judgment after the lapse of more than six years, the institution of proceedings within the six year limit will preserve his rights. If he does not care to obtain judgment, he should try to get the debtor to pay something on account of the debt. This will keep the claim alive for six years from the date of the last payment on account. If the debtor is unable to pay anything on account, the creditor should try to obtain from him a written promise to pay the debt, which will have the same effect as a payment on account in saving it from being barred. If the debtor refuses to make a written promise, a verbal promise will answer the same purpose, but the danger in relying on a verbal promise is that the debtor may afterwards deny that he gave it. In order to overcome a possible denial, the creditor should arrange to meet the debtor in the presence of witnesses, who should carefully note what the debtor says and afterwards draw up and sign a memorandum setting forth the time, place and circumstances of the acknowledgment. This memorandum will be needed, perhaps, to refresh the memory of the witnesses in later years. The acknowledgment should be clear and definite, and the debt should be carefully specified. The debtor's attention should be called to the exact amount owing by him. It is unnecessary to make the debtor agree to pay interest, for if he promises to pay the original debt, the courts will imply a promise to pay interest thereon.

What has been said about the enforcement of a promise to pay an outlawed debt applies equally to a promise to pay *a debt which has been released under seal*. If a creditor chooses to

forgive his debtor, and executes a sealed release of the debt, the creditor's legal rights are gone. If the debtor afterwards promises to pay the money, the courts will enforce this promise without requiring proof of any new consideration. The past consideration which was furnished by the creditor when the original debt was first contracted will suffice to make the subsequent promise enforceable.

Again, *where creditors enter into a composition agreement* and the debtor is freed from his obligations to them upon payment of only a portion of their claims, he may, perhaps, afterwards promise to pay one or more of them the unpaid balance. He was under no legal obligation to the creditors who took part in the composition after paying them the percentage which they agreed to take in settlement. A new promise to give one of the creditors the unpaid balance of his original claim relates back to the origin of that claim, and is enforceable although supported only by a past consideration.

Again, *where a man has been discharged in bankruptcy*, his subsequent promise to pay one of his former creditors the balance of the creditor's claim is enforceable. We shall see in the fourth part of this book that a man who complies with the Bankrupt Act of 1898 may be discharged from his obligations to his creditors. Even though a creditor has received nothing out of the bankrupt estate, his right against the bankrupt is gone. If the bankrupt afterwards promises to pay the amount of the creditor's claim, that promise is enforceable without any fresh consideration, for it is supported by the past consideration upon which the creditor's former claim, since discharged by the bankruptcy proceedings, was originally founded.

The cases just mentioned present the feature of the revival of a claim which has been legally barred by the giving of a new promise without any new consideration. In addition to these cases, there are a few other Pennsylvania decisions in which the courts have enforced a promise which was founded on a past consideration. In these other cases, a different situation presents itself. Where the promisee has in the past rendered services for the promisor under circumstances which have not been quite sufficient to create an implied contract, a subsequent prom-

ise to pay for those services has been declared enforceable without any new consideration. There are only a few Pennsylvania cases of this kind, and one of them may be mentioned as a specimen.

λ In the case of *Landis v. Royer* (1868), 59 Pa. 95, it appeared that Landis had a house built by Peter Wertz, who was to furnish all the materials. Royer sold Wertz lumber which was used in building the house. Wertz was unable to pay Royer, and Landis promised to pay the debt. When sued on this promise he defended on the ground that he had received no consideration in exchange for it. The court enforced the promise by reason of the past consideration which consisted of the supplying of materials for the house. A benefit derived from the unsolicited services of another, which the other was not bound to render, sometimes creates a moral obligation to pay for the services. If they have been volunteered without any request from the party for whom they were rendered, the value of them cannot be recovered on the theory of an implied contract. The courts will, however, in a very meritorious case, seize upon a subsequent promise as giving rise to an express contract, and they will support this promise upon the past consideration of the services previously rendered. When Royer sold the lumber to Wertz, he acquired no personal claim against Landis, but he knew that the lumber was to form part of the house which was being built for Landis. The idea to be gathered from this case is that Royer's position was very meritorious, and that the courts took advantage of the promise given by Landis to hold the latter personally liable for the lumber sold to Wertz. He would not have been personally liable unless he had made this promise. He received no consideration at the time he gave it, but the furnishing of the lumber which went into his house was a past service inuring to his benefit, and constituted a past consideration.

Rule 9.—Consideration is needed in certain cases, even where the contract is under seal.

Most contracts derive their enforceability from consideration, rather than from a seal. In most cases where a per-

son binds himself to do something for another, he expects to get something in return for what he is to give. Comparatively few enforceable promises are entirely gratuitous, depending solely upon a seal for their enforceability. Many important agreements, however, are sealed, even though there is an interchange of consideration. It adds to the solemnity of a contract to have it executed under seal, and hence many contracts are sealed which would be quite as enforceable without any seal. The parties are only thinking of the exchange of consideration when they enter into the contract, and pay little heed to the fact that it is drawn up with seals.

Under these circumstances the promisor, who expects to get a certain consideration for his promise, cannot be compelled to fulfil his promise if the promisee refuses to furnish the consideration agreed upon, even though the promise in question was made under seal. Suppose the promisor signs and seals a note for the payment of \$500 at a future date. Suppose the note is given in payment for a machine, which the promisee agrees to sell. The machine is claimed by a third person, who proves that the promisee never had any title to it. The promisor has to give up the machine to this unexpected claimant, but is sued, nevertheless, upon the note by the promisee. It would be absurd to hold him bound by his promise merely because it was made under seal, since the only real motive that led to the making of the promise was the consideration of the machine. As an actual consideration was contemplated, and this consideration has failed, the promise is not enforceable, even though the note did not specify for what it was given. If, however, the note was made in the form of a negotiable instrument, and the promisee indorsed it before maturity to an innocent holder for value, the defense which would be good against the promisee would not be good against the holder to whom he indorsed it. The holder, moreover, could recover on the note against the promisor, whether or not the note was under seal. This last peculiar doctrine will be treated at length in the second part of this book, where the subject of negotiability is to be covered.

Sealed contracts in restraint of trade are not enforceable, even though the parties intended the seal to be a legal sub-

stitute for consideration. The reason of this is that such contracts are not in favor with the courts, whose policy is to encourage competition. Certain contracts in general restraint of trade are held to be altogether void, and usually it is only when the restraint is merely partial, and is based on a sound reason that the courts will enforce it at all. If B, a shopkeeper, is selling out to C, the latter may properly require that the good will of the business which he is purchasing shall not be interfered with afterwards by B. It is proper, therefore, for the retiring shopkeeper to agree not to compete with his successor, say within a radius of one mile of the shop. This promise is in partial restraint of trade, but the courts will enforce it, since to do otherwise would be to prevent the man who is selling out from getting the full value of his good will. He is given a consideration for the promise, since it is one of the terms of the contract of sale, and is supported by the agreement of the new proprietor to pay the price asked for the business and good will.

Let us suppose, now, that the sale has been completely carried out, without any promise from the retiring proprietor not to seek business from his old customers. Suppose that the newcomer bought only the stock and fixtures, and that nothing was said about the good will. If afterwards the former proprietor gratuitously promises not to do business within one mile of his old shop, the promise is not enforceable, even though under seal. The courts will not recognize any substantial reason for enforcing the promise. The promisor did not need to make it, in order to dispose advantageously of what he sold to the promisee. He chose to give the sealed promise freely, and since he got no return for it, the courts will not lend their aid in enforcing an agreement which even partially restrains competition.

In closing this chapter on Seal or Consideration, it may be well to mention that if a promise which was made without either seal or consideration is kept by the promisor, the law will not assist him to get back what he has voluntarily given. If one promises to give a friend \$10, without seal or consideration, that promise is not enforceable. Nevertheless, if the

money promised is actually paid over to the friend, there is no good reason for the courts to make him return it. The general rule is that where one person begs or demands money from another, and the latter chooses to pay it, he will not be helped by the courts in getting it back again. This rule applies even if the payment was made to avoid a lawsuit. The man from whom money is claimed unjustly should refuse to pay it. He must not weakly yield to the demand, and then bring suit expecting the courts to assist him in recovering his money. If he has been forced to hand it over at the point of a pistol, or if it has been extorted from him by threats of injury to his property, he will be enabled to get it back. Likewise, where money has been paid under a mistake concerning a matter of fact to one who is not justified in receiving it, or where the payment has been induced by fraud. As a general rule, however, it may be stated that one should not pay money which another demands with the expectation of recovering it through a lawsuit, should the demand turn out to be unfounded.

CHAPTER IV.

THE THIRD ELEMENT NECESSARY IN ALL CONTRACTS, CAPACITY OF PARTIES.

The main rule on the subject of Capacity of Parties is that, generally, everybody has legal capacity to make all sorts of contracts. We shall be largely occupied, therefore, throughout this chapter with the exceptions to the general rule just stated. There are certain classes of individuals whose power to enter into binding agreements is quite limited, but one should remember that the ordinary person has virtually full contractual capacity unless he falls under one of the exceptions to the main rule.

There are, nevertheless, a few kinds of agreements which the ordinary person is not legally capable of making. The Pennsylvania statute of February 4, 1870, forbids any person,

partnership or association to issue any policy of insurance against loss by fire or lightning without authority expressly conferred by a corporate charter. The act declares that every policy, contract or guaranty made in violation of its provisions shall be void. The effect of this act is to deprive all individuals, firms and unincorporated associations of legal capacity to make any contract insuring others against loss by fire or lightning. There is no positive prohibition on the statute books against the making of a contract of life insurance by an individual, firm or unincorporated association, but the practical effect of the statutes regulating life insurance is to restrict most of this business to such corporations as have complied with the Pennsylvania regulations. These regulations are necessary, for the very idea of insurance suggests that the persons who are insured shall be reasonably certain of obtaining the help which they bargained for, in the event of loss. It would be unwise to let everybody go into the business of insuring others without careful safeguards.

Where the legislature lays a penalty on the doing of certain kinds of business without compliance with the state regulations, it is sometimes doubtful whether disobedience merely subjects the offender to the prescribed penalty, or also makes void all contracts entered into by him in the line of business for engaging in which he has not obtained legal authority. If the legislature not merely prescribes a penalty, but also specifically declares that agreements made in disobedience to the act shall be void, the case is clear. Unfortunately, most of the Pennsylvania statutes which require licenses to be taken out or other formalities to be complied with by those who engage in certain kinds of work, do not state whether or not agreements made without compliance with the statutory provisions shall be utterly void. Such acts usually provide nothing but a penalty for disobedience. As the State of Pennsylvania requires various kinds of merchants and brokers to take out licenses before they transact business, and also regulates the qualifying of certain engineers, dentists, doctors and other professional men, this question is an important one.

The case of *Holt v. Green* (1873), 73 Pa. 198, shows the great danger which a man, who has failed to qualify for transacting a kind of business regulated by statute, runs when he seeks to enforce an agreement entered into by him in the course of this business. Holt sued Green for broker's commissions on a sale of certain machinery. He admitted that he was in the business of buying and selling machinery on commission, and that he had never obtained a United States license as a commercial broker. The act of Congress of June 30, 1864 (since repealed), required such brokers to take out and pay for a license. The act did not specifically nullify all contracts made by such brokers without a license. The Pennsylvania court, however, held that Holt could not recover his commissions. He was pursuing a business in continuing disobedience to an act of Congress. His right to commissions, therefore, rested upon his illegal acts, and these acts could not be considered a good ground for permitting Holt to recover commissions, since he had no right to perform the services rendered Green. All this shows that even a person who has the full contractual capacity of an ordinary individual ought to comply carefully with the Pennsylvania license acts before transacting certain kinds of business. These acts do not, for the most part, deprive anybody of contractual capacity, but merely impose certain conditions upon the exercise of contractual capacity in various lines of trade and professional activity. The act of February 4, 1870, goes further than the license acts, however, for it absolutely denies to all persons, firms and unincorporated associations any capacity to make certain sorts of insurance contracts.

There are five classes of individuals whose capacity to form contracts is less than that of the ordinary person. These are minors, persons mentally deficient, married women, corporations and foreigners. Taking up these five classes in the order named, we shall see how far each class has the power to enter into legally enforceable agreements.

(A) CONTRACTUAL POWERS OF MINORS.

All persons, male or female, are minors until they reach the age of twenty-one years. In legal decisions they are often called "infants." Infancy continues in the eye of the law until the age of twenty-one, even in the case of minors who have had much business experience, and who are, perhaps, better able to take care of their own rights than many persons of full age.

Minors are not totally lacking in contractual powers. Some agreements which they may make are just as binding on them as if they were past twenty-one. As regards the majority of contracts, however, which would be absolutely binding on a person who has come of age, the minor is given his choice of standing by any contract or repudiating it. His minority, therefore, makes the contract voidable as to him. While it is absolutely binding on the other party who deals with the minor (supposing the other to be of full age), the minor is free either to affirm the contract or to disaffirm it. *Such contracts are called voidable*, for although they are not entirely null and void, yet they may be avoided and set aside if the minor so desires. Later on, certain features of voidable contracts will be considered, but we shall first see about the limited number of contracts which a minor may enter into just as validly as if he had come of age.

The most important kind of contract that a minor may validly and absolutely bind himself by is a contract to purchase for himself the *necessaries* of life. If he is married, his contractual power in this respect extends to the purchase of necessaries for his wife and children, as well as for himself. A minor is allowed to bind himself legally for necessaries, because he might not get credit anywhere if the rule of law were otherwise. It would be a hardship rather than a benefit to him, if the minor could repudiate his obligation to pay for even those things of which he might stand in sore need. He might starve if he had neither money to pay for necessaries nor the privilege of binding himself by a contract to pay the price of them to one from whom he might try to buy them on credit.

The rule giving a minor power to make a perfectly valid contract for necessities does not extend further than the requirements of the case demand. *If the minor has parents, or a guardian, or anyone else who occupies for him the place of a parent, and if any such person looks after the minor and supplies him with necessities, the minor cannot legally obligate himself when he buys necessities on his own account.* The tradesman who makes a contract with a minor always runs a certain risk. If the minor tries afterwards to set aside the contract, the tradesman will be under the burden of having to prove that the goods he sold were necessary to the minor. If it appears that the minor could have obtained these necessities without cost at his own home, the tradesman's suit usually fails. Furthermore, the tradesman must show that the things furnished by him to the minor were not excessive in quantity or extravagant in quality. The tradesman can recover only for such an amount of necessities as were reasonably required by the minor in question. If he has charged the minor too high prices, he can recover only the fair value of his goods.

No list of necessities can be made out which will apply to all minors. Questions of wealth, social position, training, health, and in general all the surrounding circumstances help to determine what may be regarded as necessary for any particular minor. Food, clothing, shelter, and a reasonable amount of education are needed by all. Likewise, medicine, nursing and medical attendance during periods of illness. A minor who is learning to be an artist will need instruction, books, paints and a variety of articles required to carry on his studies. If he has a very large estate, a reasonable amount of foreign travel may be a "necessary," especially if it is recommended either to help forward his education or to improve his health. A farmer's son, who lives in a lonely part of the country, may be considered to need a horse, although the son of a city man with the same pecuniary prospects would be in no such need. If, however, the city boy were in delicate health the horse might be a necessary for him, should his means warrant it. On the other hand, a city boy usually requires more education than a country boy. If the minor is without anybody

to provide for his wants, and is too young to look after himself at all, a third person may supply his wants, and hold the minor's estate liable. A third person who advances money with which the minor buys necessities may recover his loan from the minor, because he has virtually supplied the minor with the necessities.

The doctrine allowing persons under twenty-one to make valid contracts for necessities is usually *confined to personal necessities*. What may be required in order to take proper care of the minor's property does not fall within this doctrine. Suppose a minor goes into the book business, and needs a quantity of books in order to replenish his shelves. This is not a personal requirement, and the man who sells him books runs a great risk, for the minor is free to repudiate the transaction. Where the minor buys things for his home, or for the farm on which he lives, it is often hard to draw the line between what are properly necessities and what are not, as appears from the case of *Mohney v. Evans* (1865), 51 Pa. 80. Evans had been living with his mother, who was also his guardian. He bought two oxen from Mohney, for use in hauling upon the farm, in order to help support his mother, himself and the other children. The guardian took charge of the oxen with full knowledge of her son's purchase, and without making any objection. They were used upon the farm for a time, and then traded for a horse, which afterwards did the hauling instead of them. When Mohney called for his money a year later the guardian and her son refused either to pay it or to restore the oxen. Evans could not be held liable simply because he had parted with the oxen. The mere fact that a minor has consumed, or otherwise disposed of goods which he has received does not prevent him from escaping liability to pay for them, if he is sued for the price, unless the goods were necessities. If the goods were not necessities, he must return them or pay the price, in case he still has them. In the suit against Evans, the court decided that the cardinal question, whether or not the oxen were necessities, could not be answered by any arbitrary rule of law. It required to be passed upon by a jury, who would look into all the circumstances. What the jury finally decided

does not appear from the law reports, but the case is noteworthy, since it shows that sometimes articles may be considered as necessities which are not directly needed for the minor's personal use. The jury may have considered that the oxen were reasonably necessary to help run the little farm which supplied Evans with food.

If a minor becomes engaged to be married, and breaks the engagement before reaching the age of twenty-one, *he cannot be held liable for breach of promise*. Nevertheless, should the minor actually wed, the marriage cannot usually be set aside on the ground of infancy. Even where the marriage has actually taken place, it is said not to be binding if one of the parties is under the age of twelve, unless the marriage relation is maintained until the party in question has passed that age. The law in Pennsylvania, however, is not clearly settled on this point.

The act of April 8, 1833, directs that *no minor shall have the power of making a will*. This applies to married as well as to unmarried persons.

The act of June 7, 1887, allows minors to take and hold shares in, or to make loans to *any co-operative association* established under that act, or to deposit money with any such association. The association may pay the minor any money due him in these transactions, and the minor's receipt will be valid. The act of May 18, 1893, makes a similar provision for minors who may become interested in co-operative banking associations formed under the same act of 1893. The act of June 24, 1897, makes it lawful for minors who have attained the age of eighteen to enter into all needful contracts for becoming members of *fraternal and beneficial societies* lawfully organized and doing business under the laws of Pennsylvania. There are a number of other Pennsylvania statutes about minors, most of which have to do with regulating the employment of them in stores and factories. These latter acts have very little bearing on a minor's contractual capacity, but employers of labor should study them carefully, and note the penalties imposed for disobedience. Something is said on this subject in the twentieth chapter.

From what has just been stated you will see that there are very few kinds of contracts which a minor may make with perfect validity. It is dangerous even to turn over property to a minor which has been left to him under the terms of a will, or to which he has fallen heir. Suppose a friend has left a minor some money, and the friend's executor is asked to pay it over either to the minor himself or to his father. The executor should insist on having a guardian appointed by the Orphans' Court. The receipt of any other person does not completely protect the executor, unless the will dispenses with the necessity of appointing a guardian. If any contract needs to be made regarding property in which the minor is interested, it is usually desirable to have it made on behalf of the minor by his guardian. If the minor has no guardian, one should be appointed for him by the Orphans' Court, even though his parents are living. This is not necessary in the case of contracts for apprenticing a minor, which will be considered in the seventh chapter.

We have seen that when the minority of a party to a contract prevents the contract from being absolutely binding, it is called *voidable*. The minor has a right to disaffirm it. This right may be exercised at any time before the minor reaches twenty-one, and afterwards within such a further period as may be considered reasonable. If the minor comes of age, and afterwards does anything which clearly shows an intention to affirm the contract, he cannot later on disaffirm. If, for instance, he has extravagantly bought a tally-ho at the age of twenty, and continues to use it for many months after coming of age, he has thereby affirmed the purchase. He cannot afterwards return the tally-ho, although it was not a "necessary," and get back his money. Assuming, however, that he destroyed it in an accident before coming of age, he may recover the money he paid for it after reaching twenty-one, unless he wilfully or recklessly destroyed it, or unless he has affirmed the purchase since arriving at full age. If, in the latter case, he waited a very long time before demanding the money, his tacit acquiescence would amount to an affirmation. If he destroyed the property wilfully or recklessly he is liable

for the wrong which he has committed, for we shall see later that every minor is responsible for such wrongful acts, which are called torts.

What constitutes a reasonable period, within which the minor may, after reaching his majority, disaffirm a contract, always depends on the circumstances of the particular case. In the tally-ho case, suppose the minor continues to use the tally-ho after coming of age. His conduct in so doing for several months may properly be considered as a ratification of the contract. If the tally-ho was accidentally burned before the minor reached twenty-one, his mere omission to demand his money back for a year would be less evidence of any intention to ratify than the actual use of the tally-ho for several months, as in the former supposition. Finally, suppose that the contract made during minority was to be performed in the future, and that the minor neither paid the price nor received the tally-ho. His failure after passing twenty-one to take any measures respecting the contract would be evidence against ratification rather than in favor of it, because the minor would have nothing in this last case to undo and set aside. His silence under such circumstances would betoken disaffirmance rather than affirmance. Needless to say, a direct express statement from the former minor that he intends to affirm is always more satisfactory to the other party than mere silence or other conduct which may seem to indicate affirmance. It is often wise for the other party to get the former minor to sign a written affirmance of the contract after coming of age.

Although mere silence will not usually bar the right to disaffirm until a long time has passed after the minor comes of age, yet silence may destroy the right to disaffirm when the former minor by failing to speak out has knowingly given the impression that no disaffirmance is intended. This is seen in the case of *Logan v. Gardner* (1890), 136 Pa. 588. A woman aged twenty signed a deed for three acres of land. The purchaser sold the land to a third person, and finally it was conveyed to Gardner and others. Fifteen years after she had signed the deed, the woman sued to eject Gardner and the others from the land. The passage of fourteen years since she

had come of age would not necessarily defeat her rights, because the term of twenty-one years is sometimes allowed for the assertion of rights to real estate, although only six years are usually allowed in the case of personal property. Her inaction during this long period of time greatly weakened her case, but the decision against her was mainly rested on the following facts. Seven years after she reached full age she learned that the man who was then in possession of the land which she had previously sold was spending over \$3,000 in drilling oil wells and erecting fixtures. Despite her knowledge of what he was spending, she let him go ahead without a word of objection. The Supreme Court said that her silence at that particular time would not have told against her if she was ignorant of the improvements which were being made on the land. Since, however, she was aware of them, she was under a duty either to speak out and disaffirm her deed then, or else to hold her peace forever after. Her silence under the circumstances was equivalent to a positive affirmance of the contract which she had made when under twenty-one, for it would only encourage fraud to permit her to disaffirm afterwards. This case presents the feature of estoppel, for the woman was estopped, that is, precluded from asserting her rights, by her conduct which was inconsistent with such an assertion. The doctrine of estoppel is frequently applied where a person has helped to mislead others to their disadvantage, and afterwards attempts to assert rights against them which are inconsistent with the position which the person pretended or at least seemed to occupy.

If a minor makes a voidable contract, and after coming of age promises to fulfil it, the promise is not binding unless made to the other party who entered into the contract or his agent. *Chandler v. Glover* (1859), 32 Pa. 509.

If a minor makes a contract, and, after he comes of age, states that he intends to live up to it, he is bound by this ratification, *even though he was ignorant of his right* either to affirm or disaffirm. One exception to this rule is made in surety contracts, about which the rules of law are very strict. Suppose a boy of eighteen signs his name as surety for a friend. Sup-

pose he is told after reaching twenty-one that the friend has failed, and that he must stand the loss, and promises to do so. He is not liable on this affirmation, unless aware at the time that he was free to repudiate the surety contract on the ground that his minority when he made it rendered the contract voidable.

One who deals with young persons should be careful to see whether they are under or over twenty-one years. *If a minor has the appearance of being over twenty-one* his legal power to contract is no greater than if he looks his real age. Even if he falsely represents that he is of age, the rule is the same, because the minor cannot give himself contractual capacity merely by telling a lie. The other party, however, who is injured by the minor's deception may recover damages which he sustains on account of the fraud, although he cannot really enforce the contract. To illustrate this distinction, suppose the minor orders goods on credit from a shopkeeper, and the latter discovers before sending the goods off that the minor's statement about being of full age was untrue. Let us assume that the goods are not necessities. The shopkeeper could not collect anything from the minor if he went ahead, and delivered the goods, for the minor could not be held against his own wishes to keep his promise that he would pay for the goods. He is not liable on the contract. Neither could he be held liable in an action for damages based on his fraud, since the shopkeeper's prompt discovery of the fraud saved him from suffering any damages on that account. The subsequent delivery of the goods was made with a knowledge of the real facts and was not based on the minor's deceitful statements. Now suppose that the shopkeeper's discovery of the minor's age was made after the goods had been delivered. The shopkeeper could not recover on the contract, but he could get damages for the wrong done to him through the minor's deceit.

There are many other wrongful acts besides deceit for the consequences of which a minor may be held liable. If he recklessly injures another's person or property, he must pay damages. He is responsible for the utterance of slander, or for publishing libels. *These acts of wrong-doing are called torts, and minority is no excuse for the one who commits them.* A

minor, however, is not liable for torts committed by his agents, unless done under his direction. A full grown person is liable not only for the torts which he commits himself, but also for those done by his employees in the course of their service for him. As a minor has not full contractual capacity to employ agents, it follows that he may escape the consequences of torts committed by them.

Suits on contracts and suits for damages arising out of torts are both civil suits, and are distinguished from criminal proceedings. It may be well to say a few words about *the minor's capacity to commit crime*. It is often stated that nobody is criminally responsible until he is seven years old. From seven until fourteen, he is supposed to be incapable of meriting punishment as a criminal, but this incapacity may be disproved by evidence of premature development of the mental and moral faculties. From fourteen to twenty-one he is supposed to be capable of crime, but this supposition may be disproved by evidence that the minor is very backward, and cannot distinguish between right and wrong or harbor criminal malice. The immaturity of childhood is, of course, a different thing from the mental disorder of lunacy, which we shall take up next.

(B) CONTRACTUAL POWERS OF PERSONS MENTALLY DEFICIENT.

Under the head of mental deficiency, we include idiocy, insanity and drunkenness. Idiocy is a condition which exists from birth. Insanity is a brain disorder arising at some time after the afflicted person is born. Sometimes it does not come from any particular disease of the brain, but merely from old age, and this form of mental break-down is called senility. There are a thousand different forms of mental deficiency, but it must be remembered that a man is not lacking in contractual powers, unless he cannot reasonably understand what he is doing when he attempts to make a bargain, and so is unable to look after his own interests. A person may have a mania in one direction, but in ordinary business affairs he may be all

right. Again, many persons who are past their prime have lost something of their early mental vigor, but it would be absurd to treat their agreements as if made by persons bereft of all understanding.

Again, many binding contracts are made by persons who have just before partaken freely of intoxicants, and it would be unfair to let one of the parties set such a contract aside without clear proof that he was plainly unbalanced by drink. On the other hand, one who has degraded himself by habitual hard drinking until he has largely lost the control of his intellectual faculties, is about on a level with the insane.

The fact that there are so many different degrees of insanity, and that a man may become insane, but nevertheless continue to go about his daily business unsuspected of having lost his mind, would cause hardship if contracts made by such a person were always considered voidable. Judges are very slow to set aside a contract where the one who dealt with the lunatic had no reason to suspect his mental weakness, unless the lunatic's condition has been previously established by a decree of court which is notice to all the world. Apart from this point of difference, the rules about the contracts of persons who are mentally deficient resemble the rules laid down in the case of minors. A lunatic or habitual drunkard for whom the court has appointed a committee is in much the same position as a minor for whom a guardian has been appointed. Everybody should deal with the committee, rather than with the lunatic or habitual drunkard himself. If there is no committee, and the lunatic is not fully taken care of by his relatives and friends, he is allowed for his own advantage to make a valid contract for the purchase of necessities. The term "necessaries" has about the same meaning as in the case of minors. A person of unsound mind may contract *a valid marriage*, if he sufficiently understands what a marriage means, and also the rights and obligations which flow from it as regards the married couple themselves, their family and their property. This rule is like that which allows minors to enter into the married state, provided they know what they are doing, and understand the nature of the marriage relation.

If a man is of unsound mind, his contracts are for the most part not binding, provided either that there has been a decree of court to that effect, or else that his mental condition is apparent to the one with whom he deals. It would seem, however, that if he should subsequently recover his mind, he would have the choice of affirming or disaffirming such contracts in much the same way as would a minor on coming of age. It is, perhaps, even more risky to have dealings with a deranged person than with a minor, and where the condition of insanity or habitual drunkenness has been declared to exist by a formal decree of court, one is foolish to make any contract regarding the afflicted person or his property except with the committee appointed by the court.

(C) CONTRACTUAL POWERS OF MARRIED WOMEN.

The act of June 8, 1893, provides that a married woman shall have the same right and power as an unmarried person to acquire, own, possess, control, use, lease, sell or otherwise dispose of any property of any kind, real or personal, and either in possession or expectancy, and may exercise the said right and power in the same manner and to the same extent as an unmarried person; but she may not mortgage or convey her real property, unless her husband join in such mortgage or conveyance. Real property or realty means lands, together with houses and other fixtures built thereon and certain interests therein. All other property is called personal property, or personalty. The act of 1893 goes on to state that a married woman may, in the same manner and to the same extent as an unmarried person, make any contract in writing, or otherwise, which is necessary, appropriate, convenient or advantageous to the exercise or enjoyment of the rights and powers granted by the foregoing provision; but she may not become accommodation indorser, maker, guarantor or surety for another.

The restriction upon a married woman's powers regarding her real estate is for her husband's benefit. From very ancient times a husband has had a certain interest in his wife's realty,

which is called his right of curtesy. This right gives him the use of all her realty after her death, if he survives her, and lasts until the death of the husband himself. The Pennsylvania statutes which gradually enlarged the contractual powers of a married woman, and deprived the husband of some of his rights to her personal property, preserved his curtesy right. The law provides that the sale or mortgage of the wife's real estate shall not defeat her husband's curtesy, unless he consents to it, as by signing the deed or mortgage. If, therefore, a married woman owns land, and conveys it to a third party against her husband's wishes, the husband's curtesy right will stand, in case he survives his wife, just as if she had retained control of the property. At her death he will be entitled to the enjoyment of the land for the balance of his own life.

The other restriction on a married woman's powers which prevents her from making a binding contract as an accommodation indorser, maker, guarantor or surety, is intended for her own benefit. She is not likely to reap much advantage from such an agreement, and would in many cases lose all her property if she could validly make it. Wealthy married women might be persuaded by their husbands to guarantee all manner of contracts, in order to aid the husbands in getting credit. Most women do not understand much about these matters, and they would be readily drawn into ruinous agreements in the belief that their husbands would protect them, and that their own obligation would never amount to anything.

The act of 1893 provides furthermore that *a married woman may sue and be sued* civilly in all respects and in any form of action with the same effect and consequences as an unmarried person; but she may not sue her husband, except in proceedings for divorce, or in a proceeding to protect or recover her separate property, whensoever he may have deserted or separated himself from her without sufficient cause, or may have neglected or refused to support her; nor may he sue her, except in proceedings for divorce, or in a proceeding to protect or recover his separate property, whensoever she may have deserted him, or separated herself from him without sufficient cause. In any proceeding brought by either under this pro-

vision to protect or recover the separate property of either, both shall be fully competent witnesses, except that neither may testify to confidential communications made by either, unless this privilege be waived at the trial. See act June 4, 1901, P. L. 425.

The foregoing provisions as to suits by and against married women refer only to civil suits. It goes without saying that married women are liable like everybody else for any crimes which they may commit. In the case of civil suits brought against women, there is one advantage which, whether they are married or unmarried, they enjoy over men. In a few civil proceedings against men and boys, it is permissible to arrest the defendant and make him give bail, but females are exempted from arrest in civil suits.

(D) CONTRACTUAL POWERS OF CORPORATIONS.

In the second book the subject of corporations will be treated at length. It may be mentioned here, however, that the contractual powers of most corporations are defined and limited by their charters, and by the constitution and statute law of the states where they are formed. The limitations thus placed upon any corporation should be carefully studied by its officers, and also by those with whom it may have dealings. In the case of a corporation chartered under the laws of a foreign country or of some other state, but doing business in Pennsylvania, regard should also be paid to the laws of Pennsylvania regulating the transaction of business here by corporations organized elsewhere.

A corporation has such contractual powers as are expressly conferred upon it, and also such incidental powers as are reasonably necessary to the exercise of the powers expressly conferred. Where a corporation exceeds its powers, and attempts to make a contract clearly outside of its line of business, such a contract may be declared either voidable or void. If the corporation is a municipal corporation, as, for instance, the City of Pittsburgh, the courts usually declare such a contract absolutely void. They are not so strict in the case of a private corporation, as, for instance, a manufacturing company, and

where the contract has been largely performed, the courts are disposed to prevent either the private corporation or the other party from having it set aside. If the contract has not been even partially performed, and no rights will be prejudiced by the decision, the courts will refuse to enforce an agreement made in excess of corporate powers.

(E) CONTRACTUAL POWERS OF FOREIGNERS.

The act of May 1, 1861, allows foreigners to purchase and hold Pennsylvania real estate not exceeding in quantity 5,000 acres, or in net annual income \$20,000. This does not apply to the citizens of any state in the Union, for they have the same right to buy and hold Pennsylvania realty as have Pennsylvanians themselves. Corporations formed under the laws of our sister states, however, should not buy and hold Pennsylvania realty, unless they come within the provisions of the act of June 8, 1893, or the acts of June 16, 1893, June 1, 1881, April 17, 1889, June 24, 1895, or April 19, 1901, allowing certain foreign manufacturing and other corporations to hold certain real estate. The act of May 23, 1887, permits a foreign corporation to buy in at any sheriff's sale, or other judicial sale, any real estate upon which such corporation may have a mortgage, judgment, or other lien. Various statutes give such corporations the right to hold realty so purchased for a limited period; and from time to time the legislature has passed statutes extending such period. Foreign corporations which need real estate in Pennsylvania to carry on their business here, and which do not come within the provisions of the acts just mentioned, sometimes comply with the law by organizing a subsidiary Pennsylvania corporation under such Pennsylvania laws and with such a charter as may enable the subsidiary corporation to hold title to the real estate in question. The Pennsylvania state authorities are not disposed to institute proceedings against a foreign corporation which unlawfully acquires title to realty here, but one practical inconvenience of disobeying the law lies in the fact that the title of the corporation is somewhat under a cloud. If the corporation

ever sells the realty, this cloud may make it difficult to convey a clear title to the purchaser.

For a further discussion of foreign corporations, see Chapter XXXIV.

CHAPTER V.

THE FOURTH ELEMENT NECESSARY IN ALL CONTRACTS, REALITY OF CONSENT.

In the great majority of cases, when the parties to an agreement go through the process of offer and acceptance, the fourth element, namely, reality of consent, is present. Offer and acceptance bring the minds of the parties together, and when this happens it is only in exceptional cases that their consent is not real and genuine. When the exceptional case arises, you find that while the offer and acceptance were made, yet the agreement is not an enforceable contract by reason of the absence of the fourth element. Any one of five different things may deprive an agreement of this element. First, both the parties may have fallen into a vital mistake as to some fact, upon the supposed existence of which their agreement was founded. Second, one of the parties may have assented to the agreement by reason of misrepresentations innocently made by the other. Third, one of the parties may have been led to make the agreement by the other's fraud. Fourth, one of the parties may have been completely under the other's mastery, so that his apparent consent was no real expression of intention, because produced by undue influence. Fifth, the consent of one of the parties may have been dragged from him by the other through actual or threatened force. These five things will be treated separately.

It should be understood that the courts will not lightly nullify a contract on the ground that the consent was not genuine. When the element of offer and acceptance is shown to be present, it is usually taken for granted that the fourth

element, reality of consent, is present also, and the man who asserts the contrary must usually prove his assertion clearly and fully.

(A) MISTAKE.

Very few mistakes are sufficient to nullify an agreement. If only one of the parties labors under a mistake, he cannot blame the other party or have the contract set aside on that ground. Even where the mistake is common to both parties, it will invalidate the contract only when it relates to a supposed fact, upon their belief in which both parties based their agreement. One of the few Pennsylvania cases in which a common mistake as to a fact was held sufficient to upset a contract is that of *Jenks v. Fritz* (1844), 7 W. & S. 201. Fritz was purchasing some land from Jenks by the acre, and they both appointed a surveyor to measure it. Upon the surveyor's report that the tract of land contained 194 acres, the deed was executed and delivered, and Fritz gave Jenks bonds for the purchase money calculated in accordance with the reported acreage. Judgment was entered against Fritz upon these bonds, but he defended as to a portion of the amount claimed from him, proving that the tract really contained only 175 acres. The court allowed him to deduct a proportionate amount of the purchase money by reason of the deficiency in the size of the tract. The quantity of land sold was a material ingredient in the contract. The parties had not arrived at the price of the land by mere guess-work, and agreed to take the risk of its containing more or less than 194 acres. They had employed a surveyor, and calculated the price in exact accordance with their mistaken belief that his report was correct. When a conveyance is made without a survey, and the purchase money is paid or a bond given for it, the contract is definitely closed, and cannot be ripped open again unless the actual quantity of land conveyed differs so grossly from the estimated quantity that the courts discover evidence of deceit in the discrepancy. The subject of deceit belongs under the head of fraud. The court in the case cited was all the more ready to

listen to the allegation of mistake, since the contract had not been fully executed, and since Jenks was seeking the court's aid in his effort to make Fritz pay the price of 194 acres.

The case of *Sankey v. First National Bank* (1875), 78 Pa. 48, shows that a mistake will not vitiate a contract *unless it is of substantial importance*. Sankey sold the bank some government bonds at par, both parties believing that the government was redeeming the bonds, although in fact the time for paying them off had been postponed, and the postponement had caused the bonds to command a premium in the market. Sankey certainly would not have sold his bonds at par had he known that bonds of the same issue were selling at a premium in New York and Philadelphia. The court held, nevertheless, that the mistake or ignorance of the parties in regard to the premium was not an essential fact in connection with the contract. It was a matter of only collateral importance, and Sankey could get no relief from the court in his effort to overturn the contract. If the law had been shaped according to Sankey's desire, there would be no certainty in the sale of stocks and bonds, for a disappointed party could almost always find some fact or other regarding the security sold which was unknown to both parties at the time the contract was made, and which, he could assert, affected the value of the security.

A mistake of judgment or opinion, even though both parties labor under it, is usually no ground for setting aside a contract. Neither is a mistake of expectation as to what will happen in the future, although the case of *Miles v. Stevens* (1846), 3 Pa. 21, makes an exception to this last rule. In that case the main inducement for a contract was the expectation of both parties that the land sold under the contract was about to become the site of a great city by reason of certain expected legislation to run the Erie Canal to the land and make a harbor there. This expectation was disappointed, and when the seller sued for the purchase money it was held that, as the contract had not been fully executed, a court of justice would not enforce payment which had been promised under a common mistake as to a material fact.

A mistake or ignorance of law, even though shared by both parties, will not usually invalidate a contract. Sometimes, however, where a mistake as to law is based upon a mistake as to fact, it may prevent the contract from being enforced. In the case of *Gross v. Leber* (1864), 47 Pa. 520, it appeared that a man was administrator of the estate of his father, who had been trustee for a certain woman. He mistakenly supposed that his appointment as administrator of his father's estate necessarily constituted him also his father's successor as trustee for this woman. Under this mistake he executed a certain sealed bond, although he personally owed the woman nothing. The court held that the bond could be set aside if he gave it under a total misapprehension of his power and duties as administrator, and without intending to create a personal obligation, and upon the mistaken supposition that he was trustee for the woman, and bound in that capacity to execute the bond.

(B) MISREPRESENTATION.

Misrepresentation as here considered exists when one party to a contract innocently misleads the other as to some material fact, and so obtains the latter's consent under a misconception. In order that a misrepresentation may be made the ground for defeating a contract, it should usually be proved that the party who made it was bound to have knowledge of the truth, so as to give the disappointed party a right to rely upon what the other said. The disappointed party should prove also that the misrepresentation induced him to enter into the contract, and that he was really misled by it to his injury.

The foregoing requirements must be met also by a person who seeks to invalidate a contract on the ground of fraud. Most of what will be said under the head of fraud applies also to a case involving misrepresentation, the difference being that in the case of fraud the idea of intentional deceit figures prominently. The courts are more disposed to nullify a contract where fraud is proved, for a man who has purposely and falsely misstated matters is more blameworthy than one who was merely in error.

Care should be taken to distinguish between a misrepresentation as to a past or existing fact on the one hand, and, on the other hand, a promise that the contract shall be performed in a certain way. An instance of misrepresentation in the sale of land would occur if the land were located in a distant state, and if the seller were to tell the purchaser that it was situated in the midst of a thriving town. If the seller were himself misinformed as to this matter, and the land actually lay far off from any settlement, you would have a misrepresentation of a material fact which induced the purchaser to enter into the contract. On the other hand, suppose the contract of sale specifically provided that it should not take effect and that no payment was to be made unless at least 1,000 persons were shown to be living within a radius of one mile around the land in question. In the second case the seller's statement as to the dwellers in the vicinity of the land would be drawn into the contract and made a part of it. Being a term of the contract itself, it would be considered under the head of Offer and Acceptance, and if it were found that the land was located in an utter wilderness, performance of the contract itself, according to its very terms, would not be made by the seller of the land. In the former case where the representation as to the neighborhood of the land sold was not put into the contract, but merely helped induce the purchaser to consent, the element of reality of consent is the one which must be considered. The purchaser is not in the position of being able to tell the seller that the latter has not fulfilled the terms of the contract. If the purchaser wants to defeat the agreement as it was made, he must go outside of its terms, and prove that as a preliminary to the formation of the agreement itself, a certain misrepresentation was put forth by the seller, which induced the purchaser to give his consent. This distinction reveals the practical importance of embodying representations upon which you want to rely in the terms of the contract itself. If you fail to do this, you must bear the burden of proving that any representation about the incorrectness of which you complain actually induced you to form the contract; and, furthermore, that the other party's representation related to matters which

were more open to his observation than to yours; and that the incorrectness of his representation will result in loss to you if the contract is enforced.

Misrepresentations may be set up by the disappointed party who is sued upon a contract: first, in order to prevent it from being enforced against him; and, second, if he discovers them after the contract has been completely executed, in order to have it ripped open again, and the parties restored to their original positions, just as when the agreement was first made. The courts are more ready to entertain proof of misrepresentation when it is discovered early, and promptly utilized to prevent the enforcement of a contract, than when it is not brought to light until after the contract has been completely performed. In the former case, the disappointed party merely asks the court not to enforce against him an agreement based on the misrepresentation of the party who is seeking the court's aid. In the latter case, the disappointed party is asking the court to reopen a matter which has been already closed. If the rights of innocent third persons will be affected by upsetting the contract, the courts will hardly ever disturb it. Such third persons should not be made to suffer merely because the disappointed party was misled by the one with whom he chose to make a contract. Even where third persons are not involved, the courts hesitate to disturb a contract which has been completely executed, if it is found that intervening circumstances would prevent the restoration of the parties themselves to their original positions in case it were decided to upset the contract.

(C) FRAUD.

What has been said on the subject of misrepresentation applies also where one party has been deceived into making a contract by the other's intentional falsehood. Where the misstatement was not false to the knowledge of the party uttering it at the time when it was made, but was made with a reckless disregard as to whether it was true or untrue, it will amount to fraud. It is more serious than an innocent misrepresentation.

The party who has been deceived by the other's fraud may bring an action of deceit against the one who has wronged him, but this action cannot be maintained for a mere misrepresentation.

When the party who is wronged discovers the fraud he should make up his mind *promptly* whether to go ahead with the contract or to have it nullified. The contract is not absolutely void, but only *voidable* at the pleasure of the party defrauded, who will lose his right to set it aside if he goes ahead with it after the fraud comes to his knowledge. Suppose that the purchaser of goods induces the seller to give him a long term of credit by false statements as to his financial strength. Should the seller learn of the fraud before delivering the goods, he cannot proceed to deliver them, and then have it in his power to set aside the contract if he chooses to do so later. If they are already delivered, and the seller takes the purchaser's note for the amount due, or sues to recover judgment for this amount, after learning of the fraud, he cannot later on have the contract nullified, and demand a return of his goods. He affirms the contract by proceeding upon the idea that the goods have really become the purchaser's property, and that the purchaser's only duty is to pay the price. What the seller should do under such circumstances, if he wants to upset the contract, is to sue, not for the money, but for a return of the goods. He has a right to get the sheriff to seize the goods under a legal writ called a writ of replevin. If the seller upon learning of the fraud demands the money from the purchaser, this of itself is not such an affirmation of the contract as will bar the seller from subsequently having the goods seized. If the purchaser has in the meantime resold the goods to an innocent third person, the latter may hold them as against the original, defrauded seller.

Even if the defrauded person chooses to affirm the contract, he is not thereby prevented from deducting out of any money which he may owe to the other party such a sum as will compensate him for damages caused by the fraud. The courts, however, do not encourage a man, who keeps quiet about an alleged piece of fraud for a long time after discovering it, to

let matters run on as if he took no account of it, and finally to try to impose heavy damages on the other party. A party's right to relief against deceit depends very largely upon the promptness with which he acts after learning the true state of affairs. If a fraudulent claim is made against you, and you agree to compromise it with full knowledge of its real nature, you cannot afterwards dispute the validity of the compromise contract by asserting fraud in the original claim.

The case of *Mahaffey v. Ferguson* (1893), 156 Pa. 156, shows that the courts are not disposed to set aside contracts on the ground of fraud, unless the party who alleges it can prove that he was really misled by it to his loss. Ferguson was negotiating for the purchase of standing timber belonging to Mahaffey. The latter's agent, Marsh, had misrepresented the quantity of the timber upon the tract which Ferguson bought, but Ferguson mistrusted Marsh, and went upon the land to see about it for himself. He thus had a chance to inspect the entire tract, and several examinations were made by Ferguson's agents, but not completed on account of rain. Finally he closed the contract, but afterwards wanted it set aside because of Marsh's misstatements. The court held that although Ferguson's investigations had been incomplete, he could not complain of what Marsh had said, since he had chosen to rely on himself and his own agents.

At the conclusion of the subject of misrepresentation a distinction was drawn between misstatements which induce the making of a contract on the one hand, and promises or guaranties actually forming part of the contract itself, on the other hand. The same distinction is of importance in many cases of alleged fraud. In the course of the negotiations which lead up to a contract one of the parties may, perhaps, make false statements as to mere matters of opinion or as to what he intends doing in the future, or as to other things very remotely connected with the contract in hand. If the other party wants to hold the man who gives utterance to such expressions, so that he may legally be entitled to place reliance on them, he should insist on having them made part of the contract, and specifically agreed to by the other party. Otherwise, when he is disap-

pointed as to such matters, and tries to use them as a means of nullifying the contract, he will be told by the courts that the fraud which he alleges is not vitally connected with the contract itself. Unless he has drawn such expressions into the terms of the contract, they will be considered merely casual, collateral remarks which have no legal bearing on it. He should insist that the other party specifically agree to be bound to make good any representations, that is, to warrant them. It will be even better if the other party agrees that the entire contract is to be regarded as essentially dependent on the truth of such representations, which makes them vital conditions of the contract. We shall see more about the distinction between a warranty and a condition when we take up the subject of breach of contract in the fourth part of this book.

Sometimes the *mere concealment* of a material fact constitutes fraud, although no false statement has been affirmatively made to the injured party. Where the parties deal at arm's length, the general rule is that neither is bound to disclose anything to the other. There are occasions, however, when parties who are closely associated enter into contracts, and the confidential relation between them is such as to make the mere wilful concealment of material facts a fraud, if this leads the party who is ignorant of the facts into a contract he would not otherwise make. We shall consider some of these confidential relationships when we take up the subjects of Agency and Partnership, and especially when we look into the duties of caretakers of estates, such as trustees.

More serious than mere concealment, and akin to a false statement is any *deceitful artifice* practiced by one party to a contract on the other, in order to induce the latter to make it. One of the cases in which this kind of trickery was held to be such clear fraud as would make a contract voidable is that of *Pennock's Appeal* (1850), 14 Pa. 446. Some realty belonging to a dead man's estate was sold at auction to Pennock and another purchaser, but they learned afterwards that the price had been run up by a sham bidder employed by one of the administrators in charge of the estate. On account of this fraud the contract could not be enforced against them. In the

case of *Harner v. Fisher* (1868), 58 Pa. 453, it appeared that Fisher had owed \$96.50 to Harner, which the latter could not collect. Harner hit upon the device of employing a third person named Shorb to buy a horse on credit from Fisher, and he gave Shorb \$10 to be paid on account of the purchase. Shorb bought the horse for \$95, paying \$10 down, and he agreed to pay Fisher the balance of the purchase money, \$85, in a few days. Harner got the horse from Shorb, giving him the claim for \$96.50, which Shorb took to Fisher as payment of the balance due on the horse. Fisher would not accept the claim, offered to restore the sum of \$10 to Shorb and finally sued to recover the horse. The court allowed him to get it back, for a creditor has no more right than anybody else to defraud a debtor into parting with property. If Fisher had agreed to sell the horse to Harner himself, and had delivered it and afterwards sued for the price, it would be perfectly right for Harner to set off Fisher's debt to him against his debt to Fisher. In that supposition, if Harner had acted squarely the court would not have allowed Fisher to get his horse back or to collect the price of it from Harner, since he owed Harner more on another account than Harner owed him on account of the horse. Harner, however, forfeited his right to set off his own claim against Fisher, because he had obtained the horse by a scheme to entrap the latter, which was fraudulent. This made the contract to sell the horse voidable, and Fisher chose to nullify it upon discovering the fraud.

Many points involving fraud are treated in the following paragraphs under the head of Undue Influence.

(D) UNDUE INFLUENCE.

Undue influence is a mixture of fraud, which we have just treated, and force, which we shall treat next in order. If one person gains a mastery over another, any contract which the latter may enter into under the former's domination does not possess the element of reality of consent. While the first element, offer and acceptance, may be present, yet the consent of the party who cannot resist the other, and think and act for

himself, is not the genuine expression of his own will. It really represents the controlling will of another, rather than that of the party who seemingly enters into the contract.

In order to set aside a contract on the score of undue influence, the proof must be clear and convincing. The mere fact that the consent of one party was obtained through the constant nagging and importunity of the other, or of the other's friends, is insufficient to show that the party who was finally induced to make the contract had ceased to be his own master. Sometimes a man of slightly weak will makes a contract in order to get rid of the wearisome persistence of the other party. Such a man cannot escape the consequences of his agreement, except by establishing that the other party's superior will power had completely overcome his own. The courts are reluctant to permit a contract to be overthrown on the ground of undue influence, unless the parties were so closely associated as to give one the fullest chance to exercise it over the other. A mere acquaintance can hardly acquire this influence, but it is often acquired by one member of the same household over another, especially where the latter's mental faculties are not robust. It will thus be seen that questions of capacity to contract may become involved with this subject of undue influence. A man who would be regarded as having just enough mental capacity to make ordinary contracts may in some cases repudiate a contract entered into by him with, say, a business associate who has acquired mastery over him, and abused this power to secure an unfair and selfish advantage.

Undue influence is brought up more frequently as a means of contesting the *wills* of persons who have died than as a means of setting aside contracts. In the fifth book we shall mention this subject in connection with wills. The matter is of importance also in the case of *gifts*. If undue influence is employed to obtain a gift, the gift may be taken back by means of appropriate legal proceedings. Again, if this influence is abused so as to make the person who is subject to it put some of his property in trust either for the one who exerts the influence or his friends, the *trust* may be defeated. What has been

said about defeating transactions inspired by undue influence applies also to gifts made or trusts created through fraud. One practical difference between setting aside gifts, trusts or contracts procured by undue influence, on the one hand, and those tainted by fraud, on the other hand, occurs where the fraud was participated in by both parties to the contract, and was aimed at the creditors of the party who disposed of his property. In the case of undue influence, the party who was a victim of it may, on escaping from it, himself seek to annul the contract. Again, where one party to a contract is the victim of the other's fraud, he may himself set on foot proceedings to annul the contract on the ground of fraud. If, however, he is a party to the fraud himself, and has conspired with the other party to the transaction to cheat his creditors, he will not be allowed to avail himself of his own fraud in order to defeat the gift, trust or contract. The creditors, however, may attack the transaction, and expose the fraud. This is frequently done where the creditors learn that their debtor has transferred a large part of his assets to his wife or to some other relative or friend on the very eve of bankruptcy. In several such cases where a wife has innocently received a transfer of her husband's property without knowledge of the intended wrong, the Pennsylvania courts have compelled restitution for the benefit of the husband's creditors. See the case of *Blum v. Ross* (1887), 116 Pa. 163.

(E) FORCE.

Needless to say, when a man enters into a verbal or written agreement, because the other party threatens to shoot him unless he does so there is no real contract. Force may also be employed in a less violent way, as where one party obtains the other's consent by kidnapping him, and keeping him under lock and key until the agreement is made. Even where a person has been arrested under legal process and imprisoned in a state or county jail, a contract which he makes in order to secure his release will be voidable, if it appears that the imprisonment was brought about for the express purpose

of extorting money. The contract is voidable, even though the prosecutor who seeks to enforce it had just and reasonable grounds for causing the other party's arrest, because the courts do not want criminal proceedings to be invoked for the mere purpose of securing money. This holds true although the prosecutor has a right to receive the money from the other party. We shall see under the heading, Legality of Object, something about the validity of a contract to settle a criminal prosecution, where the accused has not been thrown into prison. At present we are touching on the subject only to see what degree of force or constraint will make a contract voidable.

The word "*duress*" is usually employed in treating this topic, instead of "force." Force, as here used, must not be understood as necessarily pointing to bodily violence. Mere threats to injure your person or property may constitute such force as will invalidate a contract entered into by you. The courts will take into account the age, sex and condition of life of the person threatened, and relieve him from liability if they find that he was deprived by the threats of his freedom of will, even though no such effect would have been produced on a bolder person. In the case of *McGrory v. Reilley* (1879), 8 W. N. C. 104, it appeared that a woman had signed a contract at the instance of one who threatened that in case of her refusal her husband would be imprisoned for twenty years. This constituted force.

A mere fear of a lawsuit will not justify a person who is threatened with legal proceedings, and who makes a contract in order to escape them, in asserting subsequently that he was forced into making it. He should determine to resist the proceedings when he is first threatened with them, for the courts do not like a man to settle with another, and try afterwards to back out of his agreement. This matter was treated under the fourth rule regarding consideration. Usually, even where criminal proceedings are threatened, you should not compromise with the person who threatens to prosecute you, and expect afterwards that the court will help you to get your money back. Agreements for compromising certain criminal

proceedings cannot be enforced by the prosecutor, as we shall see under the next heading, but this is because such agreements lack the fifth element, legality of object, since the courts will seldom declare in such cases that the force of moral constraint has been so applied as to deprive the agreement of reality of consent.

CHAPTER VI.

THE FIFTH ELEMENT NECESSARY IN ALL CONTRACTS, LEGALITY OF OBJECT.

Nothing can be plainer than the proposition that the courts will not lend their aid to accomplish a wrong. It follows that where an agreement has an illegal object it is no contract, because it is not enforceable at law. Apart from agreements which have a positively vicious and illegal object, there are some agreements which have a perfectly innocent object, but which were certainly never intended to be enforced at law, and which, therefore, do not possess the fifth element, Legality of Object. A purely social engagement made by two persons to dine or walk together would lack the fifth element, for if the engagement were broken, the disappointed party would have no redress in a court of law. The parties never contemplated that they would enter into a strict legal relation towards each other, giving rise to contractual rights and obligations. Aside from purely social agreements and those of a similar character, which are outside the sphere of governmental intervention, pretty much every agreement possesses the fifth element, unless it has a positively vicious object in view. It remains, therefore, only to note the various classes of wrongful objects which the courts condemn.

There are three different classes of agreements which lack the fifth element: (A), those which violate the Constitution or the statute laws of the United States or of the State of Pennsylvania or Federal treaties; (B), those which interfere with

the proper conduct of government in any of its branches; (C), those which tend to injure the public as a body, or to wrong some particular member thereof.

(A) AGREEMENTS VIOLATING CONSTITUTIONAL OR STATUTE LAW OR FEDERAL TREATIES.

Taking up the first class of illegal agreements, it is obvious that the courts will not enforce an agreement which runs directly counter to a provision of the Constitution or the statute laws either of Pennsylvania or the United States or to a treaty made between our country and a foreign nation. In the case of *Millerstown v. Frederick* (1886), 114 Pa. 435, a borough was sued on a bond which it had issued in payment of debts incurred contrary to the provisions of the Pennsylvania Constitution. The State Constitution forbids a municipality from incurring indebtedness above seven per cent of the assessed valuation of its property. It was decided that even an innocent holder of bonds issued under such circumstances cannot recover on them, for they are totally void. There are countless laws which may invalidate agreements formed in disobedience to them, but it will suffice to mention a few of the most important.

The Pennsylvania statute of April 22, 1794, forbidding the transaction of worldly business on *Sunday*, makes unenforceable business agreements entered into on that day. The courts will enforce such an agreement, however, if it has been recognized by the parties as valid on a subsequent week-day. Thus, if an agreement to sell a horse is made on Sunday, and the purchaser pays some money on account later in the week, this ratification of the Sunday agreement cures it of any defect. A deed signed on Sunday is valid if delivered to the purchaser on a week-day. It is unwise merely to date a Sunday contract as if it had been made on a week-day, for there should be something actually done on a week-day to show an intention to adopt the Sunday agreement. If there is a ratification on a week-day, it makes no difference whether or not

the contract is dated as of a Sunday. There is a slight tendency to treat this provision of the act of 1794, relating to Sunday contracts, as merely an obsolete blue law, but, nevertheless, it is far preferable to make business contracts on a week-day. The sale and delivery of ice on Sunday has been held to be a matter of necessity, and so outside the scope of the act. A Sunday contract in aid of a church or other charity or concerning matters apart from worldly business affairs is not affected by the statute. For instance, a Sunday contract whereby a man hires a carriage in order to visit his father is enforceable. A will made on Sunday is valid. All contracts, as well as wills and deeds, may be validly made on any *legal holiday*. If a legal holiday falls on Sunday, however, the provisions of the act of 1794 apply, as outlined above.

Another section of the same act of 1794 provides that nobody shall be compelled to pay *gambling debts*, and that every contract, note, bond, judgment, mortgage, or other security or conveyance whatsoever made in performance of a gambling transaction shall be utterly void.

In most cases of illegal agreements, if the parties choose to perform voluntarily what they have promised to do, the courts will not upset the transaction, and restore the parties to their original condition. The courts will neither enforce the agreement nor, if the parties have fulfilled it, force them to undo what has been already done. Where, however, a man has paid a gambling debt he may bring suit against the winner within ten days to recover what he has lost. If a stakeholder is appointed pending the decision of a bet, the loser may notify him to return what was staked, and may hold the stakeholder personally liable if he pays the winner after getting such a notice.

If you lend money to anyone, in order to enable him to gamble, you cannot recover it, if you make the loan in furtherance of the illegal transaction. If you merely have knowledge of the use to which the borrower intends to put the money, and lend it to him without any purpose of encouraging him to gamble, you are not a guilty participant in the illegal transaction, and can recover your money.

Another distinction which has been drawn by the courts is that between *bucket shop transactions* in stocks and grains, on the one hand, and investments on margin, on the other hand. In a bucket shop the customers merely bet with the proprietor on the fluctuations of market prices. There is no real sale or purchase of the securities or commodities concerned. On the contrary, when an investor or speculator goes to a legitimate broker, and orders him to buy, say, twenty shares of Pennsylvania Railroad stock or a hundred bushels of wheat on margin, the broker really fills the order, and there is a perfectly legal contract of sale. The mere fact that the broker lends his customer a large part of the purchase money does not invalidate the contract, any more than if a real estate agent were to lend the purchaser of a house four-fifths of the purchase money upon mortgage.

Another statute which affects many contracts is that of May 28, 1858, providing that *the lawful rate of interest* where no express contract is made for a less rate *shall be six per cent per year*, and that no higher rate shall be charged. This act provides further that when a higher rate has been agreed upon, the debtor shall not be required to pay the excess above six per cent. If he pays, say ten per cent, he may bring suit within six months from the time of payment to recover the excess of four per cent. The defense of usury is not good as against a holder of negotiable paper taken in the usual course of business, and without knowledge of the excessive rate of interest charged the debtor. In this respect, there is a difference between a negotiable instrument given in payment of a gambling debt and one which is defective merely because excessive interest is charged. In the gambling transaction the language of the act of 1794 makes the negotiable instrument absolutely void, even though it is transferred to a holder for value without knowledge of how it originally came to be made. In the case of a gambling transaction relating to stocks, however, it would seem that a negotiable instrument given in the course of such a transaction is valid in the hands of an innocent holder for value. The subject of negotiable paper is treated at length in the second part of this book.

The act against usury was framed to prevent the oppression of poor debtors, and an *exception* to it has been made by the act of March 6, 1903, in certain cases where the borrowers seem not to need the protection of usury laws, and may need to borrow at the high rates which sometimes prevail in the money market. This act directs that whenever advances of money, repayable on demand, to an amount not less than \$5,000, are made upon warehouse receipts, bills of lading, certificates of stock, certificates of deposit, bills of exchange, bonds, or other negotiable instruments, pledged as collateral security for such repayment, it shall be lawful to contract for any rate of interest that may be agreed on in writing by the parties to the transaction.

Another *exception* to the act of 1858 is made in favor of building associations. These associations serve the useful purpose of helping thousands of people to buy their own homes. They collect dues from their members in small instalments, and in order to stimulate the members to pay punctually, interest on arrearages may be charged at the rate of two per cent per month. It often happens that a building and loan association or a mutual savings fund association will have more applications for loans than can be satisfied with the funds on hand. In order that the association may be helped, and that no applicant may be unjustly preferred over another, the act of June 4, 1901, allows the various applicants to bid for the loan, and the one offering the highest premium gets it. Such bids must be in writing, and can be received only in open meeting. When a man pays a premium for a six per cent loan, he is practically being charged over six per cent on the money which he gets. This is allowed in the case of such associations, although the courts are on the alert to prevent the charging of interest above six per cent by any similar round-about method in the case of ordinary contracts.

(B) AGREEMENTS INTERFERING WITH THE
PUBLIC GOVERNMENT.

The second class of contracts which lack legality of object are those which interfere with the proper conduct of government in any of its branches, executive, legislative or judicial. For instance, a contract guaranteeing the removal of an United States post-office to a certain store is void, because it savors of corrupt influence. So is an agreement to obtain a pardon for a convicted criminal, or to procure certain legislation. Public affairs are to be regulated by the laws enacted for that purpose, and the courts are opposed to letting the regular course of procedure be interfered with by any selfish interests, such as would be created by private contracts concerning such matters.

An agreement to pay money for stifling a criminal prosecution is void in the case of most crimes. It tends to obstruct justice, if someone who is concerned in the prosecution of a criminal bargains with him about suppressing the legal proceedings. The act of March 31, 1860, emphasizes this principle by making it a misdemeanor to take money or other reward, or the promise thereof, for compromising or concealing any treason, murder, arson, forgery, counterfeiting, burglary, robbery, larceny, kidnapping, bribery, perjury and certain other crimes. Quite apart from this act making such agreements misdemeanors, the courts would declare them unenforceable as being against public policy. There are some criminal proceedings which are more of a private nature, concerning some particular citizen rather than the entire commonwealth at large. While all citizens are interested in having a murderer brought to justice, on the contrary a prosecution for an assault and battery concerns principally the man who is injured. If this man agrees not to push criminal proceedings in consideration of being paid a sum of money, the agreement to pay him the money is enforceable. Likewise, a prosecution for obtaining money by false pretences may be compromised by a binding contract which will enable the prosecutor to get judgment for the amount promised him through a civil lawsuit on the compromise contract.

(C) AGREEMENTS INJURIOUS TO THE PEOPLE
AT LARGE OR TO PARTICULAR INDIVIDUALS.

The third class of agreements which have an illegal object are those tending to injure the public as a body or some particular member thereof. A prominent example of such agreements is one *which aims to destroy competition*. This matter is to some extent regulated by the act of Congress known as the Sherman Act. The Sherman Act, however, is limited in its operation to such monopolies as restrict interstate commerce. Long before this act was passed, the judges refused to enforce agreements in restraint of free competition. The case of *Coal & Coke Co. v. Jutte* (1904), 210 Pa. 288, is a recent illustration of some of the rules on this subject. Jutte was a miner and shipper of coal, which he marketed by boats plying on the Monongahela, Ohio and Mississippi rivers. He sold out his business to the Coal & Coke Co., and was instrumental in inducing other parties whose mines, like his, were in the Monongahela Valley, to do likewise. Jutte agreed not to engage again, individually or through any partnership or corporation, in the business of mining or shipping coal, in the territory traversed by the three rivers above named and their tributaries, for the period of ten years. Similar agreements were signed by the other concerns which sold out to the Coal & Coke Co. Later Jutte organized companies to carry on business in violation of the agreement, and the Coal & Coke Co. obtained an injunction restraining him from engaging, directly or through partnerships or corporations, in the mining or shipping of coal on the Monongahela river within the State of Pennsylvania for the remainder of the ten-year period. Jutte's defense that the agreement violated the Sherman Act was upheld in so far as the contract sought to restrain competition in commerce between Pennsylvania and other states along the Ohio and Mississippi rivers.

The contract was enforced so far as it related to the doing of business in Pennsylvania, because it did not put an unreasonable restraint upon Jutte. The courts consider the circumstances under which any such agreement is formed, and are

guided thereby in deciding whether or not to enforce it. When a man in Jutte's position is selling out his business, he can often get a better price if a term can be inserted in the agreement of sale legally binding the seller to keep out of the territory where he has been engaged, at least for a limited space of time. If the courts refused to enforce an agreement of this kind many persons retiring from business would be unable to get the fair value of their good will, for the purchasers could not tell but that those who had sold out to them would open up again in the same neighborhood, and retain all their old trade. It is allowable, therefore, to make an agreement in partial restraint of competition which is reasonable under the circumstances. An agreement to sell a retail shop in a small town may properly provide that the seller must not open up a rival shop in the same town. It would be unreasonable for that particular shopkeeper to bind himself not to engage in the same business in any part of Pennsylvania, for such a sweeping restraint would be unnecessary for the purchaser's protection. Where a provision for such a restraint is unreasonably sweeping, the courts are disposed not to restrict the seller from opening up even quite near his former stand. In the sale of concerns whose trade is widespread, the restraints imposed upon the seller may be correspondingly greater, in order to protect the purchaser in the enjoyment of the business which he buys. Where the restraint as to territory extends over the entire country, it is wise to insert a limit as to the time during which it shall last, for the courts do not want to keep a man from pursuing his particular line of business in any part of the country, and for the rest of his life. Even where the restriction as to territory is narrowly limited, a further limit as to the time during which it shall last is often inserted as a measure of precaution, especially where the man to be restricted is not selling out a business, but is merely getting employment from the people with whom he promises not to compete. Thus, a driver when he is hired to deliver milk over a certain route may validly agree, in consideration of being given employment, not to sell milk for anybody over that route for one year after the expiration of the employment.

Agreements improperly affecting domestic relations will not be enforced. The courts favor the institution of marriage, and if a husband promises his wife money for not resisting his divorce suit, the promise is unenforceable. Again, where a third person promises to pay a sum of money upon condition that the beneficiary shall obtain a divorce, the promise is not enforceable, in view of the illegal object.

An agreement tending to make a trustee or other agent violate his duty is also against public policy. Thus, where the director of a corporation is promised a sum of money for withdrawing his opposition to a transaction which is not for the corporation's interest, and for voting in favor of it, he cannot secure the aid of the courts in enforcing the promise. Even in a case which involves no such confidential relation as that of a trustee, the courts will not encourage an agreement which tends to sacrifice the rights of a third party. If you are going to bid at a sheriff's sale, and somebody who wants to keep prices down promises you money to stay away from the sale, the promise is not binding. The object of the agreement is to prevent the goods sold by the sheriff from having a fair chance in the open market. A combination of buyers to purchase for their joint account is all right, but an agreement for the mere purpose of hindering bids is void.

Likewise, any agreement made to bring about a breach of contract has an illegal object, and is unenforceable. If the illegal agreement is voluntarily carried out, the party who is injured by the consequent breach may recover damages from the persons who have thus wronged him. An injunction is sometimes issued to prevent labor unions from persuading their members to break existing contracts with employers. The subject of interference by unions with employers is treated in the case of *Purvis v. United Brotherhood* (1906), 214 Pa. 348, where the Supreme Court upheld the issuance of an injunction against certain high-handed measures to compel the employment of none but union men.

CHAPTER VII.

THE SIXTH ELEMENT NECESSARY IN A FEW CONTRACTS,
SPECIAL FORMALITY.

The five elements considered, one by one, in the preceding five chapters are all necessary in every single contract. There are a few contracts which require a sixth element. This additional element, Special Formality, does not dispense with the necessity of having present the five elements already considered. The contracts requiring special formality to be treated in this chapter relate to real estate, suretyship and guaranty, and apprenticeship. In the third chapter we noted, under Rule 6 about consideration, that subscriptions to corporation stock should be in writing. Corporations, especially municipal corporations, cannot validly make some agreements save in accordance with prescribed formality and procedure, but this pertains rather to corporation law than to contract law. It will be touched on in the second book. There are a few other kinds of contracts which need to be in writing, but as most of them are mentioned in appropriate places elsewhere throughout this volume they need not be treated here.

(A) SALES OF REAL ESTATE AND CERTAIN
OTHER REALTY CONTRACTS.

The most important act which prescribes a special formality to be followed in making certain contracts, whether made by individuals, partnerships, or corporations, is that of March 21, 1772. This directs that all leases for over three years from the making thereof, and all estates or interests in lands or buildings erected thereon shall have the force and effect of leases or estates at will only, unless put in writing and signed by the parties making or creating the same, or by their agents authorized in writing. The act provides that these formalities shall be observed not only in the making or creation of the leases and estates to which it refers, but also

in an assignment of them to a third party and in a release or surrender of them, unless the assignment, release or surrender is brought about by the operation of law. The reason for requiring these contracts to be in writing is found in the permanency of real estate. Most contracts about personal property are performed within a short time after being made, but many realty contracts are not finally performed until years have elapsed. During the passage of these years the parties to the contract as well as witnesses may die, and other important changes may take place. It is desirable, therefore, that most agreements about real estate shall have something of the same permanency as the real estate itself.

The act of 1772 refers not only to outright sales of lands and buildings, but also to the disposition of various interests concerning real estate. For instance, the grant of a perpetual right to enter another's land and obtain timber or coal there must be in writing, although a verbal sale of timber and farm crops has been held valid, where the timber and crops were to be promptly removed by the purchaser. Again, an agreement for a permanent right of way to pass over another's land should be in writing.

The person who is selling land, or leasing it for over three years, or parting with any other interest referred to in the act should *sign the written agreement*. If his signature is made by another at his direction and in his presence, there is sufficient compliance with the statute. The purchaser, tenant, or any other person who is receiving a transfer of an interest in realty need not sign. While, however, only the party disposing of real estate need sign a memorandum of the agreement, yet this party cannot waive the omission of his own signature. The contract binds both parties or neither, and where, for instance, an agreement to sell a house is signed by the purchaser, but not by the seller, the latter may not dispense with the requirement of the statute, and compel the purchaser to pay the price. No technical form of words is required, but the memorandum should identify the land to be conveyed, and state the consideration and the other contractual terms.

Where a verbal agreement is made in disregard of the act of 1772, and the person who is to get the real estate or an interest in it goes into possession of it, proceedings to evict him may be taken at the other party's pleasure, for the statute makes him only a tenant at will. In a few hard cases, however, the courts have enforced verbal agreements in spite of the act, in order to prevent flagrant injustice. Suppose you have by verbal agreement bought land in a farming country, fully paid for it, built a flour mill, and made arrangements with the neighboring farmers to grind their wheat. If the seller afterwards tried to oust you as a mere tenant at will, he would not be allowed to do so.

Even where an agreement which is defective under the act of 1772 has not been irrevocably executed, and where the parties can be restored to their original position, the courts will often give *damages to the disappointed party*. These damages are only to cover losses which the party who relies on the act of 1772 may have caused the other party by delaying to state that he would not go ahead with the agreement. For instance, suppose you have agreed verbally to buy Smith's house for \$2,000. You proceed to have the title searched, and a deed drawn up, but when you ask Smith to sign the deed, he refuses to do so on the ground that the previous unwritten agreement of sale is not binding on him. Assuming that the house is worth \$3,000, you could not recover from Smith the value of your bargain, \$1,000, for that would be practically enforcing the agreement. You could recover only, say, \$20 or \$30, to cover the expenses incurred by you before you learned of Smith's intention to repudiate the agreement on the legal, but dishonorable, excuse that it failed to comply with the act of 1772. If you had paid \$100 on account of the purchase money, you could recover that also.

(B) TRUSTS AS TO REAL ESTATE.

The act of April 22, 1856, provides that all declarations or creations of trusts of any real estate, and all grants and assignments thereof shall be proved by writing, signed by the

party holding title thereto, or by his last will in writing, or else be void. The act makes an exception in favor of cases where a conveyance of real estate is made by which a trust arises or results by implication or construction of law, or is transferred or extinguished by act or operation of law. The case of *McCloskey v. McCloskey* (1903), 205 Pa. 491, shows the workings of this statute. A son of William McCloskey, named Charles, and the heirs of John McCloskey, another son of William, brought proceedings to enforce an alleged verbal trust. They asserted that William had left almost his entire estate to his wife for life, and after her death to his three daughters, and that he had informed his children that the will was so drawn in order to protect John and Charles, who were insolvent. They averred that he agreed with the daughters that two-fifths of the estate were to be held in trust for John and Charles. The court held that such a trust in lands cannot be proved save by writing.

A trust is defined as a right of property, real or personal, held by one for another's benefit. In studying the act of 1856, we are concerned only with trusts as to real estate. The person who holds the right of property, called the legal title, is known as a trustee. The beneficiaries, for whose advantage the trust was created, are called *cestuis que trustent*. These three French words are applied where there is more than one beneficiary, a single beneficiary being called a *cestui que trust*. In the fifth book we shall see about the duties of trustees, and the various purposes for which trusts are created. The act of 1856 applies mainly to cases where the owner of land wants to bestow it upon some relative or friend, and merely states by word of mouth that he will hold it thereafter in trust for the object of his bounty.

Under the exception to the act of 1856, there are several kinds of trusts regarding realty which it does not affect. In certain situations the law implies a trust, without regard to any writing on the subject, and sometimes even against the wishes of those who are held bound as trustees. However, the act of June 4, 1901, P. L. 425, in certain cases protects third parties to whom the trustee sells or mortgages the land or

who get judgment against him. An implied trust arises where there is an actual conveyance of land, and the purchaser pays for it with his own money, but takes title in the name of another. In that case, the person in whom the legal title is put holds it merely as trustee for the real purchaser, and the latter gets the beneficial enjoyment of the property. Again, where a person who has charge of another's funds, uses them to buy realty, taking the title in his own name, he becomes by operation of law a trustee for the person with whose money he made the purchase. Again, where several persons club together to pay the purchase money, and the title is taken in the name of one alone, a trust arises for the benefit of the others to the extent of their contributions. While it is well to understand about these exceptions to the act of 1856, the safest rule to follow is to insist upon having all agreements and understandings respecting realty fully put in writing, and signed by all the parties concerned.

(C) CONTRACTS REDUCING AN ABSOLUTE CONVEYANCE TO A MORTGAGE.

The act of June 8, 1881, provides that no defeasance to any deed for real estate, regular and absolute upon its face, shall have the effect of reducing the deed to a mortgage, unless the defeasance is made at the time the deed is made, and is in writing, signed, sealed, acknowledged and delivered by the grantee of the deed to the grantor, and is recorded in the office for recording deeds and mortgages in the county where the real estate lies, within sixty days from the execution thereof.

The word "defeasance" usually means an instrument which "defeats" the force or operation of some deed. If you read over a mortgage you will see that it contains towards the beginning a conveyance from the owner of the mortgaged property, but the absolute character of this conveyance is diminished by a condition which you read a little later. The condition usually provides in the case of mortgages to secure loans of money that the mortgage shall be of no effect, if the owner of the property repays the other party the loan for which

the mortgage in question has been made. Now suppose that the parties agree that a conveyance shall have only the effect of a mortgage, but that they omit the provision restoring full title to the borrower of the money upon his repayment of the loan. Suppose the fulfilment of this condition is trusted to the lender's honor, and the agreement reads like an outright conveyance to the purchaser. This omission may cause heavy loss, for the courts will not enforce a verbal agreement reducing to a mortgage what seems on its face to be an absolute conveyance.

It is far better to have a mortgage transaction made in the regular way, for then the owner who mortgages his property may clear up his title simply by fulfilling the condition which appears on the face of the mortgage, and which usually refers to the repayment of a loan with interest. The act of 1881 allows, however, one way of drawing up the papers, besides the usual method of setting everything forth in a single document called a mortgage. This other method, which is permissible but very rarely to be recommended, may be gathered from the foregoing statement of the act. Suppose A is lending \$1,000 to B, upon the security of B's farm. The ordinary way of securing A would be for B to sign a mortgage, reciting the facts, and providing that A should have no further claim against the farm upon B's repayment of the loan at the time fixed, with interest. If, however, the parties wanted to put the transaction in the other form permitted by the act of 1881, they would proceed as follows: B would sign a deed absolutely conveying the title to A. At the same time A would sign a defeasance, setting forth that the seemingly absolute conveyance was actually only a mortgage transaction, and that B would regain a clear title to his farm upon returning the money loaned by A, with interest. This defeasance would have to be signed, sealed, acknowledged and delivered by A to B. It would also have to be recorded in the county where the farm is situated. The time allowed for the recording is sixty days, but B would have it recorded immediately, if he were prudent.

(D) CONTRACTS OF SURETYSHIP AND GUARANTY.

The act of April 26, 1855, provides that no action shall be brought to charge any executor or administrator on any promise to answer damages out of his own estate, or to charge anybody on any promise to answer for another's debt or default, unless the agreement, or some memorandum or note thereof, shall be in writing, and signed by the party to be charged therewith, or by some other person whom he has authorized. In the fourth book we shall take up the subject of suretyship and guaranty contracts, and we shall find that the courts interpret them narrowly. The reason for this is that while a person should be held fully responsible for his own obligations, he ought not to be made liable for another's debts without clear proof that he agreed to assume them. Another reason is found in the fact that many persons will rashly agree to become liable for the fulfilment of a friend's obligations with much less reflection than they give to undergoing immediate personal liability. They lightly believe that the friend will get through successfully, and that his sureties will never need to give a second thought to the remote responsibility incurred by them. This foolish way of thinking proves the ruin of many.

The act of 1855 does not apply to cases where the party who is sought to be held on a verbal promise has promised to pay what is really his own debt. Thus, if you order goods to be sent to another, but charged to your account, your promise to pay for them need not be in writing. You are not agreeing to answer for another, where you yourself become the principal debtor. Again, where the promise to pay another's debt is taken in exchange for the obligation previously owed by the other, and the latter is relieved from all liability, it does not fall under the act of 1855. The man who agrees to substitute himself for the old debtor becomes the principal debtor, and his unwritten promise binds him.

The act of 1855 does not apply where there is a transfer of funds by one person to another, and the latter promises to

use them in paying a debt due by the former to a third person. This principle is illustrated in the case of *Stoudt v. Hine* (1863), 45 Pa. 30. Stoudt obtained a power of attorney from a contractor named John Kallahan to collect money due Kallahan, who was in debt to Hine. These three men agreed verbally that \$372 should be paid to Hine by Stoudt out of the funds collected for Kallahan. Hine was permitted to enforce Stoudt's verbal promise to pay him this money, because the promise was not to make the payment out of Stoudt's own funds. He was not a surety for Kallahan, but merely agreed to turn \$372 of Kallahan's money over to Hine.

The statute of 1855 does not affect a contract to be responsible for a sum less than \$20. Compare this with the act of May 10, 1881, which directs that no person within Pennsylvania shall be charged as an acceptor on a bill of exchange, draft or order drawn for the payment of money, exceeding \$20, unless his acceptance shall be in writing, signed by himself or his lawful agent. In the tenth chapter of this book we shall see more about the liability of an acceptor of bills of exchange and other orders, for the act of 1881 relates mainly to negotiable instruments, which are treated in that chapter.

No particular form of agreement is necessary under the act of 1855, but the surety's promise to answer for another's debt or default must appear with reasonable certainty from the written instrument itself. It is not necessary that the consideration received by the surety should be mentioned in writing. The case of *Moore v. Eisaman* (1902), 201 Pa. 190, shows that, while the courts do not insist on any set words, yet they will refuse to enforce an agreement which cannot be gathered from the memorandum signed by the party to be charged with liability. Moore & Bro. made a contract with B. F. Long, who took it to Eisaman. The latter wrote at the end thereof, "O. K.," and signed his name after these letters. He was afterwards sued as surety for Long, and Moore offered to prove by verbal testimony that Eisaman had agreed to become Long's surety, and had written the letters "O. K." in order to express this agreement in writing. The court held that these two initial letters were insufficient under the act of

1855. If it had been shown that "O. K." signifies in commercial usage a guaranty by one party of another's undertaking, the court would have decided differently, because any abbreviations of words, or other short cuts to express an idea which are in common vogue, will be recognized by the courts as equivalent to more careful forms of expression. The most, however, that could be claimed for the testimony offered by Moore was that in the particular case before the court the letters "O. K." meant the same thing as a formal guaranty contract. This virtually made Moore's entire case hinge upon the verbal testimony as to what Eisaman had agreed to when he signed his name to the document.

The act of 1855 specifically refers to promises made by an executor or administrator to answer damages out of his private fortune for claims against the estate of which he is in charge. In the fifth book we shall consider what liabilities are imposed on those who wind up the estates of the dead. It will suffice here to say that, even where an executor or administrator receives consideration for promising to pay debts incurred or legacies bequeathed by the decedent, the promise is not binding unless made in writing.

The subject of suretyship and guaranty is treated at length in Book Fourth.

(E) CONTRACTS OF APPRENTICESHIP.

The act of September 29, 1770, provides that every minor who shall be bound by agreement of indenture to serve as an apprentice at any useful art or trade, with the assent of his or her parents, guardian or next friend, or with the assent of the Overseers of the Poor and approbation of any two justices, shall be forced to serve during the time agreed. It is provided that in the case of a girl the agreement should terminate the apprenticeship at or before the age of eighteen years, and in the case of a boy at or before the age of twenty-one. The case of *Phelps v. Railway Co.* (1881), 99 Pa. 108, explains the word "indenture" in the act of 1770 as meaning an agreement under seal. It was decided in this case that the agreement must also

be signed by the parties making it. The minor need not sign it, but his parents should do so, if they are acting for him, and the person, firm or corporation to whom he is apprenticed should also sign and seal the contract. The statute of 1770 mentions certain other persons who may act for the minor, usually only where the parents are dead or unable to provide for him. The contract should specifically state that the apprentice is to be taught the art or trade for which he is bound to his master. Where a guardian has been appointed to take charge of the minor, the contract is not valid unless executed by him. *Guthrie v. Murphy* (1835), 4 Watts 80.

Contracts of apprenticeship are not so common as formerly. They are used sometimes in the case of pauper children who may be bound out by those having them in charge, namely, the Overseers of the Poor. Where there is an apprenticeship, the compulsory education act and the factory laws must be complied with. The act of April 10, 1905, makes it compulsory to send children between the ages of eight and sixteen years to school, except in certain cases. The act of May 2, 1905, regulates the employment of children in industrial establishments. This act is referred to again on page 286.

PART II

THE OPERATION OF CONTRACTS.

CHAPTER VIII.

A CONTRACT WHEN FORMED USUALLY OPERATES ONLY ON THOSE WHO ARE PARTIES TO IT.

In part first of this book we have seen how a contract is formed, and now we must ask about its operation. The effect of a contract is to create legal rights and corresponding obligations. In this second part, we shall see who may exercise contractual rights, when they have been created, and against whom contractual obligations may be enforced.

Since the formation of a contract is brought about through the voluntary agreement of the parties, it follows that a third person cannot be subjected to a contractual obligation against his will. A and B have no legal power to make a private agreement which will cast a contractual liability on C's shoulders. This is easy to understand, but it is, perhaps, hard to grasp the second rule on the subject, namely, that outside persons do not acquire legal rights under a contract. This principle is frequently illustrated in cases where a concern which has been in business retires, and the new concern which succeeds it agrees to pay all outstanding debts. Suppose the creditors of the old concern learn of this arrangement, and sue the newcomers. They cannot avail themselves of the contract to which they are not parties. It was not made for their advantage, and the old concern is the only one possessing a legal right under the contract to compel its successor to pay off the debts.

An exception to the rule that no outsiders acquire legal rights under a contract exists where a trust fund is set apart by the terms of the contract for the benefit of an outsider.

Vary the case stated above by assuming that the old concern left certain assets in charge of its successor to be used by the latter for paying off the debts in question. Here you have the successor put in the position of a trustee for the benefit of the creditors of the old concern, and they can bring suit on this kind of agreement, even though they were never parties to it. The case of *Stoudt v. Hine* (1863), 45 Pa. 30, mentioned towards the end of part first, will help explain this doctrine.

CHAPTER IX.

AFTER THE FORMATION OF A CONTRACT, RIGHTS AND OBLIGATIONS CREATED BY IT MAY SOMETIMES BE PASSED TO OUTSIDERS BY SUBSEQUENT AGREEMENT OR BY OPERATION OF LAW.

(A) ASSIGNMENT BY SUBSEQUENT AGREEMENT.

Since a contract is a voluntary agreement, it is clear that the parties may change it at any time before it is finally performed, if they all consent to the change. If yesterday A and B made a contract, to-day, the contract still being unperformed, they may both legally agree with C that he shall take B's place, and that B shall have no further rights or obligations under the contract. C is fully substituted for B. The contractual tie now connects C with A, and it no longer binds B.

Let us understand next how far B may substitute C in his place without A's consent, or even against A's express desire. B can never release himself from personal liability to A, merely by getting C to agree to assume that liability. Remembering therefore, that B still remains liable to A for the performance of the obligations which he undertook, let us inquire how far he may delegate to C the actual work of performance. This point came up in the case of *Galey v. Mellon* (1896), 172 Pa. 443. Galey agreed with Mellon to drill a well. Galey was to

supply all tools, cables, fuel, labor and hauling required to complete the well and to encase it. Mellon was to furnish whatever wood might be required, also the machinery and certain other things. On the day when the contract was made Galey, in consideration of \$180, assigned his interest in it to Smith Bros., who were experienced well drillers, and who did the work. Afterwards Smith Bros. sued Mellon, using Galey's name for that purpose, in accordance with legal practice. The court stated that the work contemplated by the original contract required the labor and attention of a number of men. It did not appear that Galey was especially fitted to carry it on because of his knowledge, experience, pecuniary ability or for any other reason. There was nothing of a personal nature about it, and performance by Galey himself was not an essential feature of the contract. The case of Smith Bros. against Mellon was made stronger by the fact that he had known from the beginning that they, and not Galey, were actually drilling the well, and that he had not promptly objected.

On the other hand, *there are many contracts which essentially involve the idea of personal performance by the parties who make them.* A doctor, or an opera singer, or a cook, or anybody else who is employed on account of peculiar personal qualities cannot turn over the performance of the work agreed upon to a substitute, against the employer's wishes. It is hard to draw the line between assignable contract work and that which cannot be delegated to an outsider. Hence it is often wise to insert in a contract a clause specifically setting forth whether or not this or that party may delegate to others the performance of what the contract calls for him to do.

While a party to a contract may in some cases be unable to turn over the performance of his obligations to a substitute, rights arising under a contract may usually be assigned. To illustrate this distinction, suppose you agree with B to pay him \$100 for performing a surgical operation upon you. You could legally object if B wanted to turn over the operation to Y, who has, let us suppose, bought out B's practice. You could not, however, object to B's assigning his right to receive the sum of \$100 to Y. Let us assume that the operation has

been performed, that you are notified by Y that he has bought B's claim against you, and that B also notifies you of the assignment. If you pay B after getting this notice, you are liable to pay Y the money over again, for the claim against you was legally assignable.

The assignment of claims for wages not yet earned is discouraged by the courts, for to uphold all such assignments would work great harm. Many persons who are out of work would gladly assign their right to receive wages for weeks in the future in exchange for a little food or clothing, and they would become practically the slaves of the money lenders if such agreements were enforceable at law. Moreover, an assignment of future wages by a laborer, executed when he is neither actually employed nor engaged for employment, is considered altogether too vague and uncertain to be sustained as a valid assignment and transfer of property. It has been held, however, that an assignment of future wages in payment of a debt is valid, if the wage-earner is employed or is about to be employed by any particular person, and if he directs this particular person to turn over his future wages to his creditor.

Sometimes the sale of real estate transfers to the buyer a number of rights which are appurtenant to the real estate itself. Suppose that all the owners along a certain newly opened street agree that every house to be built on that street must have a clear space of twenty feet in front. If this restriction appears on the records in the office of the Recorder of Deeds, it will bind not only the lot owners who agree to it, but also those who purchase lots from them. Such building restrictions affect the title to the lots. Suppose that two of the owners sell their lots, one selling to A, while the other sells the adjoining lot to B. If B starts to build a house right up to the front line of his lot, A may have him stopped by an injunction. Neither was a party to the original contract, but the contracting parties mutually affected the title to their respective lots, so that nobody could buy a lot free from the building restriction. Since the restriction as to B's lot was intended for the general enhancement of the value of property along the street, A may enforce that restriction as the owner of

the neighboring lot. The restrictions are made for the reciprocal advantage of the lots themselves, whoever may be the owners. Such agreements, which affect the land itself rather than the persons who originally made them, are said to run with the land.

(B) ASSIGNMENT BY OPERATION OF LAW.

When a man dies or becomes bankrupt, a person is usually appointed to take charge of his estate, if there is anything for distribution. In the fourth part of this book we shall see that the death of a party to a contract does not always terminate it, and the executor or administrator of a deceased person is often called upon to complete contracts which the decedent failed to perform fully in his lifetime. Again, where the decedent has finished what he was bound to do under the contract, and the other party owes him money, the executor or administrator succeeds to the decedent's right to collect this money. No assignment need be made or intended by the decedent, for even if he never made a will, an administrator can be appointed to whom, by the operation of the law concerning these matters, the decedent's right of action is transferred. The subject of the estates of decedents will be treated in the fifth book.

Again, where a man is forced into bankruptcy, he may wish to refuse to recognize the trustee appointed for the benefit of his creditors. Nevertheless, this trustee, who succeeds by operation of law to most of the bankrupt's contractual rights, may bring suit on many kinds of contracts, although the trustee was probably not one of the original parties to any of these contracts, and although the bankrupt will not execute an assignment of his rights under them to the trustee. The subject of bankruptcy will be considered at length in the fourth part of this book.

CHAPTER X.

NEGOTIABLE CONTRACTS.

As a general rule, any person to whom rights under a contract are assigned stands in no better position to enforce them than the person who assigned them occupied himself. The stream does not rise higher than its source, and the interest in the contract which a purchaser acquires is usually of the same value, and subject to the same defects, as if it had remained in the possession of the original party who sold it. The case of *Frantz v. Brown* (1830), 1 P. & W. 257, shows the danger of buying a right under a contract, without fully investigating its value. Brown signed a bond for the payment of £2,200 to Frantz, which Frantz, in 1820, assigned to John Garberich. The bond was given to pay for land, but Brown, in 1819, became surety in another matter for Frantz, it being agreed that whatever he might be obliged to pay in this second affair should be deducted from the amount of the bond. Brown lost a large amount of money in the surety transaction, but Garberich refused to credit this amount on the bond, saying that he had known nothing about it. The court compelled him to give the credit asked for, because he was obliged, as the assignee of the bond, to take notice of everything which might affect the existence of the debt between the original parties. It would be different if Garberich had asked Brown whether or not Brown had any defense to make to the collection of the sum of £2,200 represented by the bond, and Brown had withheld information as to the surety affair. On this supposition, if Brown knew of Garberich's intention to buy the bond, and concealed the true state of affairs regarding it, he would not be allowed to make any defense against Garberich. He would be precluded from doing so on the theory that good faith should prevent him from misleading Garberich into making the purchase and then suddenly presenting a defense which he ought to have

mentioned before. It is customary as a measure of precaution when the person to whom a bond is payable offers to sell it, for the assignee to obtain from the maker of the bond a statement that the maker has no defense against it. This signed statement is called a declaration of no set-off.

Suppose A has a claim for \$100 against B, which you desire to buy without getting from B a declaration of no set-off. Suppose that it was a perfectly valid claim at the time you bought it, but A hurries off to B, after you pay him for the claim, and induces B to settle with him. You have no right to collect a second time from B, for he did not know of the assignment when he paid A. Even if he paid A before the debt was due, you cannot blame him, for he had no reason to suspect that you were interested in the claim. Hence the importance that the assignee of a claim should get a declaration of no set-off, or should at least immediately notify the person against whom the claim is made that it has been assigned.

There is a large class of written contracts to which the foregoing remarks do not apply. *In the case of negotiable instruments, a declaration of no set-off or prompt notification of assignment is usually quite unnecessary*, for the assignee is protected by the nature of the contract from defenses arising before or after the assignment, provided he holds the written document itself. *The documents stand for their face value, when they are negotiable* instruments for the payment of money. Likewise, they are supposed to represent the goods specified in them in the case of negotiable warehouse receipts and bills of lading. These general statements must be taken subject to the rules and limitations laid down by the act of May 16, 1901, and the other acts which are set forth in this chapter.

We have seen that some contracts are not assignable at all. Of those which are assignable, some are negotiable and the others non-negotiable. A negotiable contract is assignable in a remarkable degree, for it may circulate in the business world almost like currency, and free from many defenses to which a non-negotiable contract would be subject. For instance, suppose John Smith makes the following note, which is a typical specimen of a promissory note:

\$1,000.	Pittsburgh, June 12, 1906.
One month after date I promise to pay to the	
order of Edwin Hay	
One Thousand	Dollars
at	
Without defalcation. Value received.	
Due.....	[Signed] JOHN SMITH.

The words "Without defalcation. Value received," are not necessary, but they are usually inserted. They mean that the maker has no set-off, and that he has received consideration. John Smith is called the maker of this note, and Edwin Hay is called the payee. Suppose that John Smith never received the amount of the note, or the least consideration for signing his name to it. He would be called an "accommodation" maker. Suppose that he signed the note for the accommodation of Hay, who takes it to a bank, and gets it discounted. Even though the bank cashier knew that Smith received no consideration, the bank could hold Smith liable on the note. If Hay himself sued Smith on the note, the defense of no consideration would prevent Hay from winning. The bank, however, having paid Hay for the note, is called a holder for value, and is not prevented from enforcing the agreement against Smith by knowledge that he received nothing for entering into it.

Now, suppose that Hay gave Smith consideration for signing the note, but that Smith paid Hay the sum of \$1,000, its face value, five days before the note fell due. Smith should not pay the note at any time without receiving it back, but suppose that he foolishly paid \$1,000 to Hay without obtaining the note. If Hay, after obtaining the money from Smith, took the note to the bank, and the bank cashier discounted it with knowledge that Smith had already paid it off, the bank could not recover against Smith. Its knowledge of the payment would destroy its right to recover. If, however, the bank officers were ignorant, when the note was discounted, of the fact that

Smith had already paid it off, the bank could hold Smith liable, because the note called for the payment of \$1,000, and the bank was not bound to ask Smith whether or not he had any defense to make against it. In the case mentioned, the bank would combine the three elements generally necessary as a protection against secret defenses to negotiable instruments. These three elements are as follows: *First*, it was a holder in good faith, for it did not know that Smith had already paid off the note. *Second*, it was a holder for value, for it had discounted the note. Sometimes a man who has a note against which there is a good defense will get a bank to sue on it, merely in order to prevent the defense from being legally available as against the bank. The question then arises as to whether the bank is a holder for value, or merely suing as the agent for the real owner, against whom the defense would be available. If the bank has discounted the note or allowed the former owner of it to draw checks against his deposit in the bank to the amount of the note, on the strength of his transferring it to the bank, the bank is a holder for value. On the contrary, if the bank is merely an agent for collection, the defense which would have been good as against the former holder is equally good against his agent, the bank. *Third*, it was a holder in due course of business before maturity. Promissory notes, when overdue, are no longer negotiable, and if they are assigned subsequently, the assignee takes them subject to the same defenses that could have been made against the party who assigned them.

The customary method of assigning negotiable instruments is by *indorsement*. "Indorsement" comes from the Latin word meaning "the back," and implies that the assignment is made by a signature on the back of the document. Where a note is payable to the order of the payee, the method by which he assigns, or, to use the proper technical word, "negotiates" it, is by signing his name on the back. Let us suppose first that the payee writes nothing but his name on the back, and hands the note to a purchaser. If the party to whom the note is negotiated desires to transfer it to still another purchaser, he may simply hand over the note, thus indorsed

by the payee. Perhaps the last purchaser may want the indorsement of the party who transfers it to him, and if the latter indorses his name under the payee's signature, he also incurs the liability of an indorser, which is defined in the act of 1901. Now let us suppose that the payee of a note indorses it as follows: "Pay to the order of Aaron Holt" and signs his own name after the word "Holt." The only way for Holt to negotiate the note is by signing it himself. These general remarks should be read in connection with the terms of the 1901 statute, which carefully regulates the degrees of liability undertaken by the various persons who figure in the original making and subsequent transfers of negotiable instruments.

Many kinds of *drafts* are negotiable. These instruments are slightly more complicated than promissory notes. A draft is an order by one person on another for the payment of money. The following specimen draft will illustrate the most important features of various kinds of negotiable orders to pay money, which are drawn by one person upon another and usually in favor of a third person:

\$500.	Philadelphia, Pa., June 6, 1906.
.....	Pay to
the order of Francis Rapp	
Five Hundred	Dollars
Value received, and charge same to account of	
	[Signed] IRA JONES.
To James Hill,	
Scranton, Pa.	

Ira Jones, who orders Hill to pay Rapp, is called the "drawer," because he draws on Hill. Rapp, in whose favor the draft is made, is called the "payee," for payment is to be made to him. Hill, against whom the draft is made, is called the "drawee." The foregoing form of draft may be called a *bill of exchange*, which is defined in Section 126 of the negotiable instruments act. Many persons use the word

"draft" as synonymous with "bill of exchange," but "draft" has a wider meaning. It covers not only bills of exchange but also a great variety of non-negotiable orders to pay money. For instance, many kinds of orders for transferring funds from one department of a corporation to another may be called "drafts," but not "bills of exchange." In the case of a *check*, which is one kind of draft, a bank or trust company is usually the drawee, while the depositor who signs the check is the drawer and the man to whose order the check is made payable is the payee. Bills of exchange and other forms of negotiable drafts are indorsed like promissory notes, and with much the same legal consequences.

Frequently a negotiable instrument is not made payable to the order of any named person, but is payable to the "bearer." There being no individual payee, no endorsement will be required in order to negotiate the contract, and it passes by delivery of the paper on which it is written. The same thing is true of a negotiable contract for the payment of money to a named person "or bearer," as where a note is payable to "John Smith or bearer." In either of the two cases last mentioned, there is nothing to prevent the person who first receives the negotiable instrument from indorsing it, but he may not want to do this, for the usual forms of indorsement impose a heavier liability on the party who transfers the instrument than if he merely delivers possession of it to the one who buys it from him. One of the two words, "order" or "bearer," must appear in any negotiable instrument for the payment of money, and, besides, the other requirements laid down by the act of May 16, 1901, must be fulfilled.

With these preliminary remarks we take up the study of the act of 1901. It embodies most of the Pennsylvania law on the subject of written contracts for the payment of money, when put in the form of promissory notes, or of checks or other kinds of drafts. The act is copied in full, and the subdivisions of it made by the Pennsylvania Legislature are followed here.

(A) NEGOTIABLE INSTRUMENTS ACT OF MAY
16, 1901.

DIVISION FIRST.

Negotiable Instruments in General.

ARTICLE I.

Form and Interpretation.

SECTION 1. *Requirements.*—An instrument to be negotiable must conform to the following requirements:

1. It must be in writing, and signed by the maker or drawer.
2. Must contain an unconditional promise or order to pay a sum certain, in money.
3. Must be payable on demand or at a fixed or determinable future time.
4. Must be payable to order or to bearer, and,
5. Where the instrument is addressed to a drawee, he must be named or otherwise indicated therein with reasonable certainty.

SECTION 2. *A sum certain.*—The sum payable is a sum certain, within the meaning of this act, although it is to be paid:

1. With interest; or,
2. By stated instalments; or,
3. By stated instalments, with a provision that upon default in payment of any instalment or of interest, the whole shall become due; or,
4. With exchange, whether at a fixed rate or at the current rate; or,
5. With costs of collection or an attorney's fee, in case payment shall not be made at maturity.

SECTION 3. *Unconditional.*—An unqualified order or promise to pay is unconditional, within the meaning of this act, though coupled with:

1. An indication of a particular fund out of which reimbursement is to be made, or a particular account to be debited with the amount; or,

2. A statement of the transaction which gives rise to the instrument. But an order or promise to pay out of a particular fund is not unconditional.

SECTION 4. *Determinable future time*.—An instrument is payable at a determinable future time, within the meaning of this act, which is expressed to be payable:

1. At a fixed period after date or sight; or,

2. On or before a fixed or determinable future time specified therein; or,

3. On or at a fixed period after the occurrence of a specified event, which is certain to happen, though the time of happening be uncertain.

An instrument payable upon a contingency is not negotiable, and the happening of the event does not cure the defect.

SECTION 5. *When not negotiable*.—An instrument which contains an order or promise to do any act in addition to the payment of money, is not negotiable. But the negotiable character of an instrument, otherwise negotiable, is not affected by a provision which:

1. Authorizes the sale of collateral securities in case the instrument be not paid at maturity; or,

2. Authorizes a confession of judgment if the instrument be not paid at maturity; or,

3. Waives the benefit of any law intended for the advantage of protection of the obligor; or,

4. Gives the holder an election to require something to be done in lieu of payment of money.

But nothing in this section shall validate any provision or stipulation otherwise illegal.

SECTION 6. *Validity and negotiability*.—The validity and negotiable character of an instrument are not affected by the fact that:

1. It is not dated; or,

2. Does not specify the value given, or that any value has been given therefor; or,

3. Does not specify the place where it is drawn or the place where it is payable; or,

4. Bears a seal; or,

5. Designates a particular kind of current money in which payment is to be made.

But nothing in this section shall alter or repeal any statute requiring in certain cases the nature of the consideration to be stated in the instrument.

SECTION 7. *When payable on demand.*—An instrument is payable on demand:

1. Where it is expressed to be payable on demand, or at sight, or on presentation; or,

2. In which no time for payment is expressed.

Where an instrument is issued, accepted or indorsed, when overdue it is, as regards the person so issuing, accepting or indorsing it, payable on demand.

SECTION 8. *When payable to order.*—The instrument is payable to order where it is drawn payable to the order of a specified person, or to him or his order. It may be drawn payable to the order of:

1. A payee who is not maker, drawer or drawee; or,

2. The drawer or maker; or,

3. The drawee; or,

4. Two or more payees, jointly; or,

5. One or some of several payees; or,

6. The holder of an office for the time being.

Where the instrument is payable to order, the payee must be named or otherwise indicated therein with reasonable certainty.

SECTION 9. *When payable to bearer.*—The instrument is payable to bearer:

1. When it is expressed to be so payable; or,

2. When it is payable to a person named therein or bearer; or,

3. When it is payable to the order of a fictitious or non-existing person, and such fact was known to the person making it so payable; or,

4. When the name of the payee does not purport to be the name of any person; or,

5. When the only or last indorsement is an indorsement in blank.

SECTION 10. *Terms of instrument.*—The instrument need not follow the language of this act, but any terms are sufficient which clearly indicate an intention to conform to the requirements hereof.

SECTION 11. *The date.*—Where the instrument or an acceptance of any indorsement thereon is dated, such date is deemed *prima facie* to be the true date of the making, drawing, acceptance, or indorsement, as the case may be.

SECTION 12. *When postdated or antedated. Date of title to.*—The instrument is not invalid for the reason, only, that it is antedated or postdated, provided this is not done for an illegal or fraudulent purpose. The person to whom an instrument so dated is delivered acquires the title thereto as of the date of delivery.

SECTION 13. *When holder may insert true date. Wrong date.*—Where an instrument, expressed to be payable at a fixed period after date, is issued undated, or where the acceptance of an instrument, payable at a fixed period after sight, is undated, any holder may insert therein the true date of issue or acceptance, and the instrument shall be payable accordingly. The insertion of a wrong date does not avoid the instrument in the hands of a subsequent holder in due course, but as to him the date so inserted is to be regarded as the true date.

SECTION 14. *When wanting in a material particular.*—Where the instrument is wanting in any material particular, the person in possession thereof has a *prima facie* authority to complete it by filling up the blanks therein. And a signature on a blank paper, delivered by the person making the signature in order that the paper may be converted into a negotiable instrument, operates as a *prima facie* authority to fill it up as such for any amount. In order, however, that any such instrument, when completed, may be enforced against any person who became a party thereto prior to its completion, it must be filled up strictly in accordance with the authority given and

within a reasonable time. But if any such instrument, after completion, is negotiated to a holder in due course, it is valid and effectual for all purposes in his hands, and he may enforce it as if it had been filled up strictly in accordance with the authority given and within a reasonable time.

SECTION 15. *Incomplete instrument not a valid contract.*—Where an incomplete instrument has not been delivered it will not, if completed and negotiated without authority, be a valid contract in the hands of any holder as against any person whose signature was placed thereon before delivery.

SECTION 16. *Incomplete and revocable until delivery.* *Delivery.*—Every contract on a negotiable instrument is incomplete and revocable until delivery of the instrument for the purpose of giving effect thereto. As between immediate parties, and as regards a remote party other than a holder in due course, the delivery, in order to be effectual, must be made either by or under the authority of the party making, drawing, accepting or indorsing, as the case may be; and in such case the delivery may be shown to have been conditional, or for a special purpose only, and not for the purpose of transferring the property in the instrument. But where the instrument is in the hands of a holder in due course, a valid delivery thereof by all parties prior to him, so as to make them liable to him, is conclusively presumed. And where the instrument is no longer in the possession of a party whose signature appears thereon, a valid and intentional delivery by him is presumed until the contrary is proved.

SECTION 17. *Rules of construction where the instrument is ambiguous or there are omissions therein.*—Where the language of the instrument is ambiguous or there are omissions therein, the following rules of construction apply:

1. Where the sum payable is expressed in words and also in figures, and there is a discrepancy between the two, the sum denoted by the words is the sum payable; but if the words are ambiguous or uncertain, reference may be had to the figures to fix the amount.

2. Where the instrument provides for the payment of interest, without specifying the date from which interest is to

run, the interest runs from the date of the instrument, and if the instrument is undated from the issue thereof.

3. Where the instrument is not dated it will be considered to be dated as of the time it was issued.

4. Where there is a conflict between the written and printed provisions of the instrument the written provisions prevail.

5. Where the instrument is so ambiguous that there is doubt whether it is a bill or note, the holder may treat it as either, at his election.

6. Where a signature is so placed upon the instrument that it is not clear in what capacity the person making the same intended to sign, he is to be deemed an indorser.

7. Where an instrument containing the words "I promise to pay" is signed by two or more persons they are deemed to be jointly and severally liable thereon.

SECTION 18. *Signature in trade or assumed name.*—No person is liable on the instrument whose signature does not appear thereon, except as herein otherwise expressly provided; but one who signs in a trade or assumed name will be liable to the same extent as if he had signed in his own name.

SECTION 19. *By duly authorized agent.*—The signature of any party may be made by a duly authorized agent. No particular form of appointment is necessary for this purpose, and the authority of the agent may be established as in other cases of agency.

SECTION 20. *For or on behalf of a principal.*—Where the instrument contains or a person adds to his signature words indicating that he signs for or on behalf of a principal, or in a representative capacity, he is not liable on the instrument if he was duly authorized; but the mere addition of words describing him as an agent or as filling a representative character, without disclosing his principal, does not exempt him from personal liability.

SECTION 21. *By "procuration."*—A signature by "procuration" operates as notice that the agent has but a limited authority to sign, and the principal is bound only in case the agent, in so signing, acted within the actual limits of his authority.

SECTION 22. *Indorsement or assignment by corporation or infant.*—The indorsement or assignment of the instrument by a corporation or by an infant passes the property therein, notwithstanding that, from want of capacity, the corporation or infant may incur no liability thereon.

SECTION 23. *When forged, etc.*—When a signature is forged or made without the authority of the person whose signature it purports to be, it is wholly inoperative, and no right to retain the instrument, or to give a discharge therefor, or to enforce payment thereof against any party thereto, can be acquired through or under such signature, unless the party against whom it is sought to enforce such right is precluded from setting up the forgery or want of authority.

ARTICLE II.

Consideration.

SECTION 24. *Consideration.*—Every negotiable instrument is deemed, *prima facie*, to have been issued for a valuable consideration, and every person whose signature appears thereon to have become a party thereto for value.

SECTION 25. *Value.*—Value is any consideration sufficient to support a simple contract. An antecedent or pre-existing debt constitutes value, and is deemed such whether the instrument is payable on demand or at a future time.

SECTION 26. Where value has at any time been given for the instrument, the holder is deemed a holder for value in respect to all parties who became such prior to that time.

SECTION 27. *Lien.*—Where the holder has a lien on the instrument, arising either from contract or by implication of law, he is deemed a holder for value to the extent of his lien.

SECTION 28. *Failure.*—Absence or failure of consideration is matter of defense as against any person not a holder in due course, and partial failure of consideration is a defense *pro tanto*, whether the failure is an ascertained and liquidated amount or otherwise.

SECTION 29. *Accommodation party.*—An accommodation party is one who has signed the instrument as maker, drawer, acceptor or indorser, without receiving value therefor,

and for the purpose of lending his name to some other person. Such a person is liable on the instrument to a holder for value, notwithstanding such holder at the time of taking the instrument knew him to be only an accommodation party.

ARTICLE III.

Negotiation.

SECTION 30. *Negotiation*.—An instrument is negotiated when it is transferred from one person to another in such manner as to constitute the transferee the holder thereof. If payable to bearer, it is negotiated by delivery; if payable to order, it is negotiated by the indorsement of the holder, completed by delivery.

SECTION 31. *Indorsement*.—The indorsement must be written on the instrument itself or upon a paper attached thereto. The signature of the indorser, without additional words, is a sufficient indorsement.

SECTION 32. *Must be entire*.—The indorsement must be an indorsement of the entire instrument. An indorsement which purports to transfer to the indorsee a part only of the amount payable, or which purports to transfer the instrument to two or more indorsee severally, does not operate as a negotiation of the instrument. But where the instrument has been paid in part, it may be indorsed as to the residue.

SECTION 33. An indorsement may be either special or in blank, and it may also be either restrictive or qualified or conditional.

SECTION 34. *Special. Blank*.—A special indorsement specifies the person to whom, or to whose order, the instrument is to be payable, and the indorsement of such indorsee is necessary to the further negotiation of the instrument. An indorsement in blank specifies no indorsee, and an instrument so indorsed is payable to bearer and may be negotiated by delivery.

SECTION 35. *Conversion of blank into special*.—The holder may convert a blank indorsement into a special indorsement by writing over the signature of the indorser in blank any contract consistent with the character of the indorsement.

SECTION 36. *Restrictive indorsement.*—An indorsement is restrictive which either :

1. Prohibits the further negotiation of the instrument ; or,
2. Constitutes the indorsee the agent of the indorser ; or,
3. Vests the title in the indorsee in trust for, or to the use of, some other person.

But the mere absence of words implying power to negotiate does not make an indorsement restrictive.

SECTION 37. *Rights of indorsee.*—A restrictive indorsement confers upon the indorsee the right :

1. To receive payment of the instrument ;
2. To bring any action thereon that the indorser could bring ;
3. To transfer his rights as such indorsee, where the form of the indorsement authorizes him to do so.

But all subsequent indorsees acquire only the title of the first indorsee under the restrictive indorsement.

SECTION 38. *Qualified indorsement.*—A qualified indorsement constitutes the indorser a mere assignor of the title to the instrument. It may be made by adding to the indorser's signature the words "without recourse" or any words of similar import. Such an indorsement does not impair the negotiable character of the instrument.

SECTION 39. *Conditional.*—Where an indorsement is conditional, a party required to pay the instrument may disregard the condition and make payment to the indorsee or his transferee, whether the condition has been fulfilled or not. But any person to whom an instrument, so indorsed, is negotiated will hold the same or the proceeds thereof subject to the rights of the person indorsing conditionally.

SECTION 40. *Specially.*—Where an instrument payable to bearer is indorsed specially, it may nevertheless be further negotiated by delivery ; but the person indorsing specially is liable as indorser to only such holders as make title through his indorsement.

SECTION 41. *Two or more payees or indorsees.*—Where an instrument is payable to the order of two or more payees or indorsees who are not partners, all must indorse, unless the one indorsing has authority to indorse for the other.

SECTION 42. *When drawn or indorsed to "Cashier," etc.*—Where an instrument is drawn or indorsed to a person as "Cashier," or other fiscal officer of a bank or corporation, it is deemed, *prima facie*, to be payable to the bank or corporation of which he is such officer, and may be negotiated by either the indorsement of the bank or corporation or the indorsement of the officer.

SECTION 43. *Misspelled, etc.*—Where the name of a payee or indorsee, is wrongly designated or misspelled he may indorse the instrument as therein described, adding, if he think fit, his proper signature.

SECTION 44. *To negative personal liability.*—Where any person is under obligation to indorse in a representative capacity he may indorse in such terms as to negative personal liability.

SECTION 45. *Indorsement bearing date after maturity.*—Except where an indorsement bears date after the maturity of the instrument, every negotiation is deemed, *prima facie*, to have been effected before the instrument was overdue.

SECTION 46. *Place of making presumed.*—Except where the contrary appears, every indorsement is presumed, *prima facie*, to have been made at the place where the instrument is dated.

SECTION 47. *Continuation of negotiability.*—An instrument, negotiable in its origin, continues to be negotiable until it has been restrictively indorsed, or discharged by payment or otherwise.

SECTION 48. *Indorsements stricken out.*—The holder may at any time strike out any indorsement which is not necessary to his title. The indorser, whose indorsement is struck out, and all indorsers subsequent to him, are thereby relieved from liability on the instrument.

SECTION 49. *Transfer without indorsement.*—Where the holder of an instrument, payable to his order, transfers it for value without indorsing it, the transfer vests in the transferee such title as the transferer had therein; and the transferee acquires, in addition, the right to have the indorsement of the transferer; but for the purpose of determining whether

the transferee is a holder in due course, the negotiation takes effect as of the time when the indorsement is actually made.

SECTION 50. *Negotiation to a prior party.*—Where an instrument is negotiated back to a prior party, such party may, subject to the provisions of this act, reissue and further negotiate the same; but he is not entitled to enforce payment thereof against any intervening party to whom he was personally liable.

ARTICLE IV.

Rights of the Holder.

SECTION 51. The holder of a negotiable instrument may sue thereon in his own name, and payment to him in due course discharges the instrument.

SECTION 52. *A holder in due course.*—A holder in due course is a holder who has taken the instrument under the following conditions:

1. That it is complete and regular upon its face.
2. That he became the holder of it before it was overdue, and without notice that it had been previously dishonored, if such was the fact.
3. That he took it in good faith and for value.
4. That at the time it was negotiated to him he had no notice of any infirmity in the instrument or defect in the title of the person negotiating it.

SECTION 53. Where an instrument payable on demand is negotiated an unreasonable length of time after its issue, the holder is not deemed a holder in due course.

SECTION 54. Where the transferee receives notice of any infirmity in the instrument, or defect in the title of the person negotiating the same, before he has paid the full amount agreed to be paid therefor, he will be deemed a holder in due course only to the extent of the amount theretofore paid by him.

SECTION 55. *Defective title.*—The title of a person who negotiates an instrument is defective, within the meaning of this act, when he obtained the instrument or any signature

thereto by fraud, duress or force, and fear, or other unlawful means, or for an illegal consideration, or when he negotiates it in breach of faith or under such circumstances as amount to a fraud.

SECTION 56. *Notice of infirmity.*—To constitute notice of an infirmity in the instrument or defect in the title of the person negotiating the same, the person to whom it is negotiated must have had actual knowledge of the infirmity or defect, or knowledge of such facts that his action in taking the instrument amounted to bad faith.

SECTION 57. *Defect of title of prior parties.*—A holder in due course holds the instrument free from any defect of title of prior parties, and free from defenses available to prior parties among themselves, and may enforce payment of the instrument for the full amount thereof against all parties liable thereon.

SECTION 58. In the hands of any holder other than a holder in due course, a negotiable instrument is subject to the same defenses as if it were non-negotiable; but a holder who derives his title through a holder in due course, and who is not himself a party to any fraud or illegality affecting the instrument, has all the rights of such former holder in respect of all parties prior to the latter.

SECTION 59. *Burden of proof when title is defective.*—Every holder is deemed, *prima facie*, to be a holder in due course; but when it is shown that the title of any person who has negotiated the instrument was defective, the burden is on the holder to prove that he or some person under whom he claims acquired the title as holder in due course. But the last-mentioned rule does not apply in favor of a party who became bound on the instrument prior to the acquisition of such defective title.

ARTICLE V.

Liabilities of Parties.

SECTION 60. *The maker.*—The maker of a negotiable instrument, by making it, engages that he will pay it according to its tenor, and admits the existence of the payee and his then capacity to indorse.

SECTION 61. *The drawer.*—The drawer, by drawing this instrument, admits the existence of the payee and his then capacity to indorse, and engages that on due presentment the instrument will be accepted or paid, or both, according to its tenor, and that, if it be dishonored and the necessary proceedings on dishonor be duly taken, he will pay the amount thereof to the holder or to any subsequent indorser who may be compelled to pay it. But the drawer may insert in the instrument an express stipulation negating or limiting his own liability to the holder.

SECTION 62. *The acceptor.*—The acceptor, by accepting the instrument, engages that he will pay it according to the tenor of his acceptance, and admits:

1. The existence of the drawer, the genuineness of his signature, and his capacity and authority to draw the instrument; and,
2. The existence of the payee and his then capacity to indorse.

SECTION 63. *An indorser.*—A person placing his signature upon an instrument otherwise than as maker, drawer or acceptor, is deemed to be an indorser, unless he clearly indicates by appropriate words his intention to be found in some other capacity.

SECTION 64. *When liable as indorser.*—Where a person, not otherwise a party to an instrument, places thereon his signature in blank, before delivery, he is liable as indorser in accordance with the following rules:

1. If the instrument is payable to the order of a third person, he is liable to the payee and to all subsequent parties.
2. If the instrument is payable to the order of the maker or drawer, or is payable to bearer, he is liable to all parties subsequent to the maker or drawer.
3. If he signs for the accommodation of the payee, he is liable to all parties subsequent to the payee.

SECTION 65. *Negotiation.*—Every person negotiating an instrument by delivery or by a qualified indorsement warrants:

1. That the instrument is genuine and in all respects what it purports to be.

2. That he has a good title to it.
3. That all prior parties had capacity to contract.
4. That he has no knowledge of any fact which would impair the validity of the instrument or render it valueless.

But when the negotiation is by delivery only, the warranty extends in favor of no holder other than the immediate transferee.

The provisions of subdivision three of this section do not apply to persons negotiating public or corporation securities, other than bills and notes.

SECTION 66. *Indorsement without qualification.*—Every indorser who indorses without qualification warrants to all subsequent holders in due course:

1. The matters and things mentioned in subdivisions one, two and three of the next preceding section; and,
2. That the instrument is, at the time of his indorsement, valid and subsisting.

And, in addition, he engages that on due presentment it shall be accepted or paid, or both, as the case may be, according to its tenor, and that, if it be dishonored and the necessary proceedings on dishonor be duly taken, he will pay the amount thereof to the holder or to any subsequent indorser who may be compelled to pay it.

SECTION 67. Where a person places his indorsement on an instrument negotiable by delivery, he incurs all the liabilities of an indorser.

SECTION 68. *Order of liability.*—As respects one another, indorsers are liable, *prima facie*, in the order in which they indorse; but evidence is admissible to show that as between or among themselves they have agreed otherwise. Joint payees or joint indorsees who indorse are deemed to indorse jointly and severally.

SECTION 69. *Negotiation by broker or agent.*—Where a broker or other agent negotiates an instrument without indorsement, he incurs all the liabilities prescribed by section sixty-five of this act, unless he discloses the name of the principal and the fact that he is acting only as agent.

ARTICLE VI.

Presentment for Payment.

SECTION 70. *Presentment for payment.*—Presentment for payment is not necessary in order to charge the person primarily liable on the instrument, but if the instrument is by its terms payable at a special place, and he is able and willing to pay it there at maturity, such ability and willingness are equivalent to a tender of payment upon his part. But, except as herein otherwise provided, presentment for payment is necessary in order to charge the drawer and indorsers.

SECTION 71. Where the instrument is not payable on demand, presentment must be made on the day it falls due. Where it is payable on demand, presentment must be made within a reasonable time after its issue, except that, in the case of a bill of exchange, presentment for payment will be sufficient if made within a reasonable time after the last negotiation thereof.

SECTION 72. *To be sufficient.*—Presentment for payment to be sufficient must be made:

1. By the holder or by some person authorized to receive payment on his behalf.
2. At a reasonable hour on a business day.
3. At a proper place, as herein defined.
4. To the person primarily liable on the instrument or, if he is absent or inaccessible, to any person found at the place where the presentment is made.

SECTION 73. *Proper place.*—Presentment for payment is made at the proper place:

1. Where a place of payment is specified in the instrument and it is there presented.
2. Where no place of payment is specified, but the address of the person to make payment is given in the instrument, and it is there presented.
3. Where no place of payment is specified, and no address is given, and the instrument is presented at the usual place of business or residence of the person to make payment.

4. In any other case, if presented to the person to make payment, wherever he can be found, or if presented at his last known place of business or residence.

SECTION 74. *Must be delivered.*—The instrument must be exhibited to the person from whom payment is demanded, and when it is paid must be delivered up to the party paying it.

SECTION 75. *At a bank.*—Where the instrument is payable at a bank, presentment for payment must be made during banking hours, unless the person to make payment has no funds there to meet it at any time during the day, in which case presentment at any hour before the bank is closed on that day is sufficient.

SECTION 76. *In case of death.*—Where the person primarily liable on the instrument is dead, and no place of payment is specified, presentment for payment must be made to his personal representative, if such there be, and if with the exercise of reasonable diligence he can be found.

SECTION 77. *Partners.*—Where the persons primarily liable on the instrument are liable as partners, and no place of payment is specified, presentment for payment may be made to any one of them, even though there has been a dissolution of the firm.

SECTION 78. Where there are several persons, not partners, primarily liable on the instrument, and no place of payment is specified, presentment must be made to them all.

SECTION 79. Presentment for payment is not required in order to charge the drawer where he has no right to expect or require that the drawee or acceptor will pay the instrument.

SECTION 80. Presentment for payment is not required in order to charge an indorser where the instrument was made or accepted for his accommodation, and he has no reason to expect that the instrument will be paid if presented.

SECTION 81. Delay in making presentment for payment is excused when the delay is caused by circumstances beyond the control of the holder, and not imputable to his default, misconduct or negligence. When the cause of delay ceases to operate, presentment must be made with reasonable diligence.

SECTION 82. *Presentment dispensed with.*—Presentment for payment is dispensed with:

1. Where, after the exercise of reasonable diligence, presentment as required by this act cannot be made.

2. Where the drawee is a fictitious person.

3. By waiver of presentment, express or implied.

SECTION 83. *Dishonored by non-payment.*—The instrument is dishonored by non-payment when :

1. It is duly presented for payment, and payment is refused or cannot be obtained ; or,

2. Presentment is excused and the instrument is overdue and unpaid.

SECTION 84. *Recourse.*—Subject to the provisions of this act, when the instrument is dishonored by non-payment an immediate right of recourse to all parties secondarily liable thereon accrues to the holder.

SECTION 85. *When payable.*—Every negotiable instrument is payable at the time fixed therein, without grace. When the day of maturity falls upon Sunday or a holiday the instrument is payable on the next succeeding business day. Instruments falling due on Saturday are to be presented for payment on the next succeeding business day, except that instruments payable on demand may, at the option of the holder, be presented for payment before twelve o'clock noon, on Saturday, when that entire day is not a holiday.

SECTION 86. *At a fixed period after date.*—Where the instrument is payable at a fixed period after date, after sight, or after the happening of a specified event, the time of payment is determined by excluding the day from which the time is to begin to run and by including the date of payment.

SECTION 87. Where the instrument is made payable at a bank, it is equivalent to an order to the bank to pay the same for the account of the principal debtor thereon.

SECTION 88. Payment is made in due course when it is made at or after the maturity of the instrument, to the holder thereof, in good faith, and without notice that his title is defective.

ARTICLE VII.

Notice of Dishonor.

SECTION 89. *To whom to be given.*—Except as herein otherwise provided, when a negotiable instrument has been dishonored by non-acceptance or non-payment, notice of dishonor must be given to the drawer and to each indorser, and any drawer or indorser to whom such notice is not given is discharged.

SECTION 90. *By whom.*—The notice may be given by or on behalf of the holder, or by or on behalf of any party to the instrument who might be compelled to pay it to the holder, and who upon taking it up would have a right to reimbursement from the party to whom the notice is given.

SECTION 91. *Notice by agent.*—Notice of dishonor may be given by an agent, either in his own name or in the name of any party entitled to give notice, whether that party be his principal or not.

SECTION 92. Where notice is given by or on behalf of the holder, it enures for the benefit of all subsequent holders and all prior parties who have a right of recourse against the party to whom it is given.

SECTION 93. Where notice is given by or on behalf of a party entitled to give notice, it enures for the benefit of the holder and all parties subsequent to the party to whom such notice is given.

SECTION 94. Where the instrument has been dishonored in the hands of an agent, he may either himself give notice to the parties liable thereon or he may give notice to his principal. If he give notice to his principal, he must do so within the same time as if he were the holder, and the principal upon the receipt of such notice himself [has] the same time for giving notice as if the agent had been an independent holder.

SECTION 95. *Written notice.*—A written notice need not be signed, and an insufficient written notice may be supplemented and validated by verbal communication. A misdescription of the instrument does not vitiate the notice, unless the party to whom the notice is given is in fact misled thereby.

SECTION 96. *Notice may be written or oral.*—The notice may be in writing or merely oral, and may be given in any terms which sufficiently identify the instrument and indicate that it has been dishonored by non-acceptance or non-payment. It may in all cases be given by delivering it personally or through the mails.

SECTION 97. Notice of dishonor may be given either to the party himself or to his agent in that behalf.

SECTION 98. *In case of death.*—When any party is dead, and his death is known to the party giving notice, the notice must be given to a personal representative, if there be one, and if with reasonable diligence he can be found. If there be no personal representative, notice may be sent to the last residence or last place of business of the deceased.

SECTION 99. *Partners.*—Where the parties to be notified are partners, notice to any one partner is notice to the firm, even though there has been a dissolution.

SECTION 100. *Joint parties.*—Notice to joint parties, who are not partners, must be given to each of them, unless one of them has authority to receive such notice for the others.

SECTION 101. *Bankrupt, etc.*—Where a party has been adjudged a bankrupt or an insolvent, or has made an assignment for the benefit of creditors, notice may be given either to the party himself or to his trustee or assignee.

SECTION 102. Notice may be given as soon as the instrument is dishonored, and unless delay is excused, as hereinafter provided, must be given within the times fixed by this act.

SECTION 103. *Giving notice.*—Where the person giving and the person to receive notice reside in the same place, notice must be given within the following times:

1. If given at the place of business of the person to receive notice, it must be given before the close of business hours on the day following.

2. If given at his residence, it must be given before the usual hours of rest on the day following.

3. If sent by mail, it must be deposited in the postoffice in time to reach him in usual course on the day following.

SECTION 104. Where the person giving and the person to receive notice reside in different places, the notice must be given within the following times :

1. If sent by mail, it must be deposited in the postoffice in time to go by mail the day following the day of dishonor, or, if there be no mail at a convenient hour on that day, by the next mail thereafter.

2. If given otherwise than through the postoffice, then within the time that notice would have been received, in due course of mail, if it had been deposited in the postoffice within the time specified in the last subdivision.

SECTION 105. *Due notice by mail.*—Where notice of dishonor is duly addressed and deposited in the postoffice, the sender is deemed to have given due notice, notwithstanding any miscarriage in the mails.

SECTION 106. Notice is deemed to have been deposited in the postoffice when deposited in any branch postoffice or in any letter box under the control of the postoffice department.

SECTION 107. Where a party receives notice of dishonor, he has, after the receipt of such notice, the same time for giving notice to antecedent parties that the holder has after the dishonor.

SECTION 108. *Where to be sent.*—Where a party has added an address to his signature, notice of dishonor must be sent to that address ; but if he has not given such address then the notice of dishonor must be sent as follows :

1. Either to the postoffice nearest to his place of residence or to the postoffice where he is accustomed to receive his letters ; or,

2. If he live in one place and have his place of business in another, notice may be sent to either place ; or,

3. If he is sojourning in another place, notice may be sent to the place where he is sojourning.

But where the notice is actually received by the party within the time specified in this act, it will be sufficient, though not sent in accordance with the requirements of this section.

SECTION 109. *May be waived.*—Notice of dishonor may be waived, either before the time of giving notice has arrived

or after the omission to give due notice, and the waiver may be express or implied.

SECTION 110. *Waiver.*—Where the waiver is embodied in the instrument itself, it is binding upon all parties; but where it is written above the signature of an indorser it binds him only.

SECTION 111. A waiver of protest, whether in the case of a foreign bill of exchange or other negotiable instrument, is deemed to be a waiver, not only of a formal protest, but also of presentment and notice of dishonor.

SECTION 112. *Notice dispensed with.*—Notice of dishonor is dispensed with when, after the exercise of reasonable diligence, it cannot be given to or does not reach the parties to be charged.

SECTION 113. *Excused.*—Delay in giving notice of dishonor is excused when the delay is caused by circumstances beyond the control of the holder, and not imputable to his default, misconduct or negligence. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

SECTION 114. *When not required to be given drawer.*—Notice of dishonor is not required to be given to the drawer in either of the following cases:

1. Where the drawer and drawee are the same person.
2. When the drawee is a fictitious person or a person not having capacity to contract.
3. When the drawer is the person to whom the instrument is presented for payment.
4. Where the drawer has no right to expect or require that the drawee or acceptor will honor the instrument.
5. Where the drawer has countermanded payment.

SECTION 115. *Nor to indorser.*—Notice of dishonor is not required to be given to an indorser in either of the following cases:

1. Where the drawee is a fictitious person or a person not having capacity to contract, and the indorser was aware of the fact at the time he indorsed the instrument.
2. Where the indorser is the person to whom the instrument is presented for payment.

3. Where the instrument was made or accepted for his accommodation.

SECTION 116. Where the notice of dishonor by non-acceptance has been given, notice of a subsequent dishonor by non-payment is not necessary, unless in the meantime the instrument has been accepted.

SECTION 117. An omission to give notice of dishonor by non-acceptance does not prejudice the rights of a holder in due course subsequent to the omission.

SECTION 118. Where any negotiable instrument has been dishonored, it may be protested for non-acceptance or non-payment, as the case may be; but protest is not required except in the case of foreign bills of exchange.

ARTICLE VIII.

Discharge of Negotiable Instruments.

SECTION 119. *Discharge of.*—A negotiable instrument is discharged:

1. By payment in due course by or on behalf of the principal debtor.
2. By payment in due course by the party accommodated, where the instrument is made or accepted for accommodation.
3. By the intentional cancellation thereof by the holder.
4. By any other act which will discharge a simple contract for the payment of money.
5. When the principal debtor becomes the holder of the instrument, at or after maturity, in his own right.

SECTION 120. *When secondarily liable.*—A person secondarily liable on the instrument is discharged:

1. By any act which discharges the instrument.
2. By the intentional cancellation of his signature by the holder.
3. By the discharge of a prior party.
4. By a valid tender of payment made by a prior party.
5. By a release of the principal debtor, unless the holder's right of recourse against the party secondarily liable is expressly reserved.
6. By any agreement binding upon the holder to extend the time of payment or to postpone the holder's right to enforce

the instrument, unless made with the assent of the party secondarily liable, or unless the right of recourse against such party is expressly reserved.

SECTION 121. *Where paid by party secondarily liable.*—Where the instrument is paid by a party secondarily liable thereon it is not discharged; but the party so paying it is remitted to his former rights as regards all prior parties, and he may strike out his own and all subsequent indorsements, and again negotiate the instrument, except:

1. Where it is payable to the order of a third person, and has been paid by the drawer; and,
2. Where it was made or accepted for accommodation, and has been paid by the party accommodated.

SECTION 122. *Renunciation of rights.*—The holder may expressly renounce his rights against any party to the instrument before, at or after its maturity. An absolute and unconditional renunciation of his rights against the principal debtor, made at or after the maturity of the instrument, discharges the instrument. But a renunciation does not affect the rights of a holder in due course, without notice. A renunciation must be in writing, unless the instrument is delivered up to the person primarily liable thereon.

SECTION 123. *Cancellation. Burden of proof.*—A cancellation made unintentionally or under a mistake or without the authority of the holder is inoperative; but where an instrument or any signature thereon appears to have been cancelled, the burden of proof lies on the party who alleges that the cancellation was made unintentionally or under a mistake or without authority.

SECTION 124. Where a negotiable instrument is materially altered without the assent of all parties liable thereon, it is avoided except as against a party who has himself made, authorized or assented to the alteration, and subsequent indorsers.

But when an instrument has been materially altered, and is in the hands of a holder in due course not a party to the alteration, he may enforce payment thereof according to its original tenor.

SECTION 125. *Material alteration.*—Any alteration which changes:

1. The date;
2. The sum payable either for principal or interest;
3. The time or place of payment;
4. The number or the relations of the parties;
5. The medium or currency in which payment is to be made;

Or which adds a place of payment where no place of payment is specified, or any other change or addition which alters the effect of the instrument in any respect, is a material alteration.

DIVISION SECOND.

Bills of Exchange.

ARTICLE I.

Form and Interpretation.

SECTION 126. *Form, etc.*—A bill of exchange is an unconditional order in writing, addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay, on demand or at a fixed or determinable future time, a sum certain in money to order or to bearer.

SECTION 127. *Liability.*—A bill of itself does not operate as an assignment of the funds in the hands of the drawee available for the payment thereof, and the drawee is not liable on the bill unless and until he accepts the same.

SECTION 128. *To drawees jointly.*—A bill may be addressed to two or more drawees jointly, whether they are partners or not, but not to two or more drawees in the alternative or in succession.

SECTION 129. *Inland bill. Foreign bill.*—An inland bill of exchange is a bill which is, or on its face purports to be, both drawn and payable within this State. Any other bill is a foreign bill. Unless the contrary appears on the face of the bill, the holder may treat it as an inland bill.

SECTION 130. *When drawer and drawee are the same person.*—Where, in a bill, drawer and drawee are the same

person, or where the drawee is a fictitious person, or a person not having capacity to contract, the holder may treat the instrument, at his option, either as a bill of exchange or a promissory note.

SECTION 131. *Referee in case of need.*—The drawer of a bill and any indorser may insert thereon the name of a person to whom the holder may resort in case of need; that is to say, in case the bill is dishonored by non-acceptance or non-payment. Such person is called the referee in case of need. It is in the option of the holder to resort to the referee in case of need or not, as he may see fit.

ARTICLE II.

Acceptance.

SECTION 132. *Acceptance.*—The acceptance of a bill is the signification by the drawee to the order of the drawer. The acceptance must be in writing, and signed by the drawee. It must not express that the drawee will perform his promise by any other means than the payment of money.

SECTION 133. *Written.*—The holder of a bill presenting the same for acceptance may require that the acceptance be written on the bill, and if such request is refused may treat the bill as dishonored.

SECTION 134.—Where an acceptance is written on a paper other than the bill itself, it does not bind the acceptor except in favor of a person to whom it is shown, and who, on the faith thereof, receives the bill for value.

SECTION 135. An unconditional promise in writing to accept a bill, before it is drawn, is deemed an actual acceptance in favor of every person who, upon the faith thereof, receives the bill for value.

SECTION 136. *Time allowed.*—The drawee is allowed twenty-four hours after presentment in which to decide whether or not he will accept the bill, but the acceptance, if given, dates as of the day of presentation.

SECTION 137. *When destroyed or withheld.*—Where a drawee to whom a bill is delivered for acceptance destroys the

same, or refuses within twenty-four hours after such delivery, or within such other period as the holder may allow, to return the bill accepted or non-accepted to the holder, he will be deemed to have accepted the same.

SECTION 138. A bill may be accepted before it has been signed by the drawer, or while otherwise incomplete, or when it is overdue, or after it has been dishonored by a previous refusal to accept, or by non-payment. But when a bill, payable after sight, is dishonored by non-acceptance, and the drawee subsequently accepts it, the holder, in the absence of any different agreement, is entitled to have the bill accepted as of the date of the first presentment.

SECTION 139. *General or qualified.*—An acceptance is either general or qualified. A general acceptance assents, without qualification, to the order of the drawer. A qualified acceptance, in express terms, varies the effect of the bill as drawn.

SECTION 140. *General.*—An acceptance to pay at a particular place is a general acceptance, unless it expressly states that the bill is to be paid there only, and not elsewhere.

SECTION 141. *Qualified.*—An acceptance is qualified which is:

1. Conditional; that is to say, which makes payment by the acceptor dependent on the fulfilment of a condition therein stated.

2. Partial; that is to say, an acceptance to pay part only of the amount for which the bill is drawn.

3. Local; that is to say, an acceptance to pay only at a particular place.

4. Qualified as to time.

5. The acceptance of some one or more of the drawees, but not of all.

SECTION 142. The holder may refuse to take a qualified acceptance, and if he does not obtain an unqualified acceptance he may treat the bill as dishonored by non-acceptance. Where a qualified acceptance is taken the drawer and indorsers are discharged from liability on the bills, unless they have expressly or impliedly authorized the holder to take a qualified accept-

ance, or subsequently assent thereto. When the drawer or an indorser receives notice of a qualified acceptance he must, within a reasonable time, express his dissent to the holder, or he will be deemed to have assented thereto.

ARTICLE III.

Presentment for Acceptance.

SECTION 143. *Presentment for acceptance.*—Presentment for acceptance must be made:

1. Where the bill is payable after sight or, in any other case, where presentment for acceptance is necessary in order to fix the maturity of the instrument; or,

2. Where the bill expressly stipulates that it shall be presented for acceptance; or,

3. Where the bill is drawn payable elsewhere than at the residence or place of business of the drawee.

In no other case is presentment for acceptance necessary in order to render any party to the bill liable.

SECTION 144. *Within a reasonable time.*—Except as herein otherwise provided, the holder of a bill which is required by the next preceding section to be presented for acceptance, must either present it for acceptance or negotiate it within a reasonable time. If he fail to do so, the drawer and all indorsers are discharged.

SECTION 145. *By whom and when.* *In case of death, bankruptcy, etc.*—Presentment for acceptance must be made by or on behalf of the holder at a reasonable hour on a business day, and before the bill is overdue, to the drawee or some person authorized to accept or refuse acceptance on his behalf; and,

1. Where a bill is addressed to two or more drawees who are not partners, presentment must be made to them all, unless one has authority to accept or refuse acceptance for all, in which case presentment may be made to him only.

2. Where the drawee is dead, presentment may be made to his personal representative.

3. Where the drawee has been adjudged a bankrupt or an

insolvent, or has made an assignment for the benefit of creditors, presentment may be made to him or his trustee or assignee.

SECTION 146. A bill may be presented for acceptance on any day on which negotiable instruments may be presented for payment under the provisions of sections seventy-two and eighty-five of this act. When Saturday is not otherwise a holiday, presentment for acceptance may be made before twelve o'clock noon, on that day.

SECTION 147. *When delay is excused.*—Where the holder of a bill, drawn payable elsewhere than at the place of business or the residence of the drawee, has not time, with the exercise of reasonable diligence, to present the bill for acceptance before presenting it for payment on the day that it falls due, the delay caused by presenting the bill for acceptance before presenting it for payment is excused, and does not discharge the drawers and indorsers.

SECTION 148. *Presentment for acceptance excused.*—Presentment for acceptance is excused, and a bill may be treated as dishonored by non-acceptance, in either of the following cases :

1. Where the drawee is dead or has absconded, or is a fictitious person, or a person not having capacity to contract by bill.

2. Where, after the exercise of reasonable diligence, presentment cannot be made.

3. Where, although presentment has been irregular, acceptance has been refused on some other ground.

SECTION 149. *Dishonored.*—A bill is dishonored by non-acceptance :

1. When it is duly presented for acceptance, and such an acceptance as is prescribed by this act is refused or cannot be obtained ; or,

2. When presentment for acceptance is excused, and the bill is not accepted.

SECTION 150. Where a bill is duly presented for acceptance and is not accepted within the prescribed time, the person presenting it must treat the bill as dishonored by non-accept-

ance, or he loses the right of recourse against the drawer and indorsers.

SECTION 151. *Right of recourse.*—When a bill is dishonored by non-acceptance, an immediate right of recourse against the drawers and indorsers accrues to the holder, and no presentment for payment is necessary.

ARTICLE IV.

Protest.

SECTION 152. Where a foreign bill, appearing on its face to be such, is dishonored by non-acceptance, it must be duly protested for non-acceptance; and where such a bill, which has not previously been dishonored by non-acceptance, is dishonored by non-payment, it must be duly protested for non-payment. If it is not so protested the drawer and indorsers are discharged. Where a bill does not appear on its face to be a foreign bill, protest thereof in case of dishonor is unnecessary.

SECTION 153. *The protest.*—The protest must be annexed to the bill or must contain a copy thereof, and must be under the hand and seal of the notary making it, and must specify:

1. The time and place of presentment.
2. The fact that presentment was made, and the manner thereof.
3. The cause or reason for protesting the bill.
4. The demand made and the answer given, if any, or the fact that the drawee or acceptor could not be found.

SECTION 154. *By whom to be made.*—Protest may be made by:

1. A notary public; or,
2. By any respectable resident of the place where the bill is dishonored, in the presence of two or more credible witnesses.

SECTION 155. *Extension.*—When a bill is protested, such protest must be made on the day of its dishonor, unless delay is excused as herein provided. When a bill has been duly

noted, the protest may be subsequently extended as of the date of the noting.

SECTION 156. *Place of.*—A bill must be protested at the place where it is dishonored, except that when a bill, drawn payable at the place of business or residence of some person other than the drawee, has been dishonored by non-acceptance, it must be protested for non-payment at the place where it is expressed to be payable, and no further presentment for payment to, or demand on, the drawee is necessary.

SECTION 157. *Subsequent.*—A bill which has been protested for non-acceptance may be subsequently protested for non-payment.

SECTION 158. *Bankrupt, etc.*—Where the acceptor has been adjudged a bankrupt or an insolvent, or has made an assignment for the benefit of creditors, before the bill matures, the holder may cause the bill to be protested for better security against the drawer and indorsers.

SECTION 159. *When dispensed with. Delay.*—Protest is dispensed with by any circumstances which would dispense with notice of dishonor. Delay in noting or protesting is excused when delay is caused by circumstances beyond the control of the holder, and not imputable to his default, misconduct or negligence. When the cause of delay ceases to operate, the bill must be noted or protested with reasonable diligence.

SECTION 160. *When bill is lost or destroyed.*—When a bill is lost or destroyed, or is wrongly detained from the person entitled to hold it, protest may be made on a copy or written particulars thereof.

ARTICLE V.

Acceptance for Honor.

SECTION 161. *May be partial.*—Where a bill of exchange has been protested for dishonor by non-acceptance, or protested for better security, and is not overdue, any person, not being a party already liable thereon, may, with the consent of the holder, intervene and accept the bill, *supra* protest, for the honor of any party liable thereon, or for the honor of the person for whose account the bill is drawn. The acceptance

for honor may be for part only of the sum for which the bill is drawn; and where there has been an acceptance for honor for one party, there may be a further acceptance by a different person for the honor of another party.

SECTION 162. *In writing.*—An acceptance for honor, *supra* protest, must be in writing, and indicate that it is an acceptance for honor, and must be signed by the acceptor for honor.

SECTION 163. Where an acceptance for honor does not expressly state for whose honor it is made, it is deemed to be an acceptance for the honor of the drawer.

SECTION 164. *Liability.*—The acceptor for honor is liable to the holder, and to all parties to the bill subsequent to the party for whose honor he has accepted.

SECTION 165. The acceptor for honor, by such acceptance engages that he will, on due presentment, pay the bill according to the terms of his acceptance, provided it shall not have been paid by the drawee; and provided also, that it shall have been duly presented for payment and protested for non-payment, and notice of dishonor given to him.

SECTION 166. *Maturity.*—Where a bill, payable after sight, is accepted for honor, its maturity is calculated from the date of the noting for non-acceptance, and not from the date of the acceptance for honor.

SECTION 167. Where a dishonored bill has been accepted for honor, *supra* protest, or contains a reference in case of need, it must be protested for non-payment before it is presented for payment to the acceptor for honor or referee in case of need.

SECTION 168. *Presentment.*—Presentment for payment to the acceptor for honor must be made as follows:

1. If it is to be presented in the place where the protest for non-payment was made, it must be presented not later than the day following its maturity.

2. If it is to be presented in some other place than the place where it was protested, then it must be forwarded within the time specified in section one hundred and four.

SECTION 169. *Delay.*—The provisions of section eighty-

one apply where there is delay in making presentment to the acceptor for honor or referee in case of need.

SECTION 170. When the bill is dishonored by the acceptor for honor, it must be protested for non-payment by him.

ARTICLE VI.

Payment for Honor.

SECTION 171. *Payment for honor.*—Where a bill has been protested for non-payment, any person may intervene and pay it, *supra* protest, for the honor of any person liable thereon or for the honor of the person for whose account it was drawn.

SECTION 172. *Notarial act.*—The payment for honor, *supra* protest, in order to operate as such, and not as a mere voluntary payment, must be attested by a notarial act of honor, which may be appended to the protest or form an extension to it.

SECTION 173. The notarial act of honor must be founded on a declaration made by the payer for honor or by his agent in that behalf, declaring his intention to pay the bill for honor, and for whose honor he pays.

SECTION 174. *Preference.*—Where two or more persons offer to pay a bill for the honor of different parties, the person whose payment will discharge most parties to the bill is to be given the preference.

SECTION 175. *Discharge.*—Where a bill has been paid for honor all parties subsequent to the party for whose honor it is paid are discharged, but the payer for honor is subrogated for, and succeeds to, both the rights and duties of the holder, as regards the party for whose honor he pays, and all parties liable to the latter.

SECTION 176. Where the holder of a bill refuses to receive payment, *supra* protest, he loses his right of recourse against any party who would have been discharged by such payment.

SECTION 177. The payer for honor on paying to the holder the amount of the bill, and the notarial expenses incidental to its dishonor, is entitled to receive both the bill itself and the protest.

ARTICLE VII.

Bills in a Set.

SECTION 178. Where a bill is drawn in a set, each part of the set being numbered and containing a reference to the other parts, the whole of the parts constitutes one bill.

SECTION 179. *Negotiation*.—Where two or more parts of a set are negotiated to different holders in due course, the holder whose title first accrues is, as between such holders, the true owner of the bill. But nothing in this section affects the rights of a person who in due course accepts or pays the part first presented to him.

SECTION 180. *Liability*.—Where the holder of a set indorses two or more parts to different persons, he is liable on every such part, and every indorser subsequent to him is liable on the part he has himself indorsed, as if such parts were separate bills.

SECTION 181. *Acceptance*.—The acceptance may be written on any part, and it must be written on one part only. If the drawee accepts more than one part, and such accepted parts are negotiated to different holders in due course, he is liable on every such part, as if it were a separate bill.

SECTION 182. *Delivery*.—When the acceptor of a bill, drawn in a set, pays it without requiring the part bearing his acceptance to be delivered up to him, and that part at maturity is outstanding in the hands of a holder in due course, he is liable to the holder thereon.

SECTION 183. Except as herein otherwise provided, where any one part of a bill, drawn in a set, is discharged by payment or otherwise, the whole bill is discharged.

DIVISION THIRD.

Promissory Notes and Checks.

ARTICLE I.

SECTION 184. *Negotiable promissory note*.—A negotiable promissory note, within the meaning of this act, is an unconditional promise, in writing, made by one person to

another, signed by the maker, engaging to pay on demand or at a fixed or determinable future time, a sum certain in money, to order or to bearer. Where a note is drawn to the maker's own order it is not complete until indorsed by him.

SECTION 185. *A check.*—A check is a bill of exchange drawn on a bank, payable on demand. Except as herein otherwise provided, the provisions of this act applicable to a bill of exchange, payable on demand, apply to a check.

SECTION 186. *Presentation.*—A check must be presented for payment within a reasonable time after its issue, or the drawer will be discharged from liability thereon to the extent of the loss caused by the delay.

SECTION 187. *Certification.*—Where a check is certified by the bank on which it is drawn, the certification is equivalent to an acceptance.

SECTION 188. *Discharge.*—Where the holder of a check procures it to be accepted or certified, the drawer and all indorsers are discharged from liability thereon.

SECTION 189. *Not an assignment.*—A check, of itself, does not operate as an assignment of any part of the funds to the credit of the drawer with the bank, and the bank is not liable to the holder unless and until it accepts or certifies the check.

DIVISION FOURTH.

General Provisions.

ARTICLE I.

SECTION 190. *Name of act.*—This act shall be known as the negotiable instruments law.

SECTION 191. In this act, unless the context otherwise requires:

“Acceptance” means an acceptance completed by delivery or notification.

“Action” includes counter-claim and set-off.

“Bank” includes any person, or association of persons, carrying on the business of banking, whether incorporated or not.

"Bearer" means the person in possession of a bill or note which is payable to bearer.

"Bill" means bill of exchange and "note" means negotiable promissory note.

"Delivery" means transfer of possession, actual or constructive, from one person to another.

"Holder" means the payee or indorsee of a bill or note, who is in possession of it, or the bearer thereof.

"Indorsement" means an indorsement completed by delivery.

"Instrument" means negotiable instrument.

"Issue" means the first delivery of the instrument, complete in form, to a person who takes it as a holder.

"Person" includes a body of persons, whether incorporated or not.

"Value" means valuable consideration.

"Written" includes printed, and "writing" includes print.

SECTION 192. The person "primarily" liable on an instrument is the person who, by the terms of the instrument, is absolutely required to pay the same. All other parties are "secondarily" liable.

SECTION 193. In determining what is a "reasonable time" or an "unreasonable time" regard is to be had to the nature of the instrument, the usage of trade or business (if any) with respect to such instruments, and the facts of the particular case.

SECTION 194. *Sundays or holidays.*—Where the day or the last day for doing any act herein required or permitted to be done, falls on Sunday, or on a holiday, the act may be done on the next succeeding secular or business day.

SECTION 195. The provisions of this act do not apply to negotiable instruments made and delivered prior to the passage hereof.

SECTION 196. In any case not provided for in this act, the rules of the law merchant shall govern.

SECTION 197. *Repeal.*—All acts or parts of acts inconsistent herewith be and the same are hereby repealed.

SECTION 198. *Date act is to take effect.*—This act shall

take effect on the first Monday of September, Anno Domini nineteen hundred and one.

(B) OTHER ACTS CONCERNING NEGOTIABLE
INSTRUMENTS FOR THE PAYMENT
OF MONEY.

In the seventh chapter, under the first subdivision, the act of April 22, 1794, was set forth. This act declares that any note or bill, as well as other written agreements, given for the payment of gambling debts shall be void. Negotiable instruments given for a gambling consideration are nullified, although they may have been bought by an innocent holder. An exception to this rule exists, however, in the case of a "stock gambling" transaction; a negotiable note given therein is good in the hands of a *bona fide* holder for value, without notice and before maturity. The act of April 12, 1872, provides that when any negotiable instrument shall be given for a consideration consisting entirely or partially of the right to make, use or sell any patent, the words "given for a patent right" shall be prominently and legibly written or printed on the face of the instrument, above the signature thereto; and such instrument in the hands of any purchaser or holder shall be subject to the same defenses as in the hands of the original owner or holder. If, however, a negotiable instrument which is given for a patent right does not contain notice of the fact, it will not be subject to secret defenses in the hands of an innocent holder for value. The person who takes, sells, or transfers any such negotiable instrument which fails to comply with the act of 1872 may be fined \$500 and imprisoned for sixty days, provided he has knowledge of the character of the consideration. The act of May 10, 1881, provides that no person within Pennsylvania shall be charged as an acceptor on a bill of exchange, draft or order drawn for the payment of money, exceeding \$20, unless his acceptance shall be in writing, signed by himself or his lawful agent. This act was mentioned in the seventh chapter under the heading, "Contracts of Suretyship and Guaranty."

(C) AN ACT CONCERNING BILLS OF LADING AND WAREHOUSE RECEIPTS.

The act of September 24, 1866, (reported in the Pamphlet Laws for 1867, Appendix, page 1363), directs that *warehouse receipts*, given for any goods, wares, merchandise, grain, flour, produce, petroleum, or other commodity, stored or deposited with any warehouseman, wharfinger, or other person, in this state, or *bills of lading*, or receipts for the same, when in transit, by cars, or vessels, to any such warehouseman, wharfinger, or other person, shall be negotiable, and may be transferred, by indorsement and delivery of said receipt, or bill of lading; and any person, to whom the said receipt or bill of lading may be so transferred, shall be deemed and taken to be the owner of the goods, wares and merchandise therein specified, so as to give security and validity to any lien created on the same, subject to the payment of freight and charges thereon; and no property on which such lien may have been created, shall be delivered by said warehouseman, wharfinger or other person, except on the surrender and cancellation of said original receipt, or bill of lading, or in case of partial sale or release, of the said merchandise, by the written assent of the holder of said receipt, or bill of lading, indorsed thereon; Provided, that all warehouse receipts, or bills of lading, which shall have the words "not negotiable" plainly written or stamped on the face thereof, shall be exempt from the provisions of the act.

This act of 1866 provides further that no warehouse receipt shall be given except for goods actually received, and that duplicate receipts shall be so indorsed. Warehousemen are forbidden to deliver goods while a receipt for them remains outstanding, for the man who stored them may have negotiated the receipt to an innocent holder, whose rights must be protected. If the receipt is lost or destroyed, the only legal way to dispense with it is to secure a decree from the Court of Common Pleas allowing the goods to be delivered to the owner of them.

PART III

THE INTERPRETATION OF CONTRACTS

CHAPTER XI.

RULES OF EVIDENCE RELATING TO CONTRACTS.

We have seen how a contract is formed. We have also seen how it operates as regards the persons on whom it imposes liabilities or confers legal rights. We now come to consider a few of the main rules about the interpretation of contracts, if they come before the courts in legal proceedings. We shall see in the present chapter a few important rules of evidence concerning the proof of contracts in court, and shall afterwards consider what construction a judge will place upon contracts where it is hard to discover the real intention of the parties.

The various points to be taken up here may be grouped around the idea that a written contract is usually far better than a verbal one, from the standpoint of practical advantage. In the seventh chapter we saw that a verbal contract is just as binding legally as a written one, except in a few cases. In the majority of cases, even where no special formality is required, a written contract is, nevertheless, preferable to one that is not written. Some of its advantages may be enumerated as follows: first, it shows that there was a definite agreement, and not merely an indecisive bargaining between the parties, which never amounted to a contract; second, it prevents perjury; third, it prevents the parties from forgetting the terms which they settled upon; fourth, the very act of putting an agreement in writing brings to light points which require adjustment, for the careful expression of a contract on paper fixes one's mind on the exact meaning of the words used; fifth, it often enables legal redress to be obtained more quickly,

for many disputes about verbal contracts involve the long delays incident to trial by jury, while they would be speedily settled by the court if they had been set forth in writing; sixth, it is more easily proved before a court.

Only the last two reasons for preferring a written contract to a verbal one need any comment. If you bring suit to enforce a verbal contract, you may find that the other party differs with you in his recollection of its terms, and the dispute of fact thus raised may have to be settled by a jury. This usually involves a delay of months, and sometimes of years. On the other hand, if the contract is fully embodied in writing, probably no such dispute can be raised by the other party. Even if he offers testimony to prove that the writing which he signed does not correctly express the intention of the parties, the courts may refuse to hear it. A rule of evidence which is being applied constantly forbids a written contract to be contradicted by verbal testimony. There are certain exceptions to this rule, but it is strictly enforced in most cases, even though it sometimes works hardship. A person who can read should not sign a paper without examining its contents, and it would open the door to fraud for judges to allow a person to excuse his failure to live up to a written contract on the plea that he was not acquainted with its contents. If you carelessly sign a contract without thoroughly understanding it, you must blame yourself for the consequences.

The sixth reason for preferring a written contract is that it can be proved more easily in court than a verbal one. Those who make a verbal contract, as well as the by-standers who witness it, may not remember the transaction clearly, or may fall sick, or die, or may live at a great distance from the courthouse where the contract is to be proved. Even if they come to court and are prepared to testify, they may be subjected to interruptions, and may be unnerved by the lawyer for the opposition. Their motives in testifying about the contract may be attacked, especially if they are interested parties. Finally, suppose that the verbal contract has not been made known to any outsider, and that one of the parties is dead or insane. The act of May 23, 1887, forbids the other party to

testify about the contract. The death or lunacy of one party seals the other's mouth. As there are no witnesses, the contract cannot be proved at all.

Not only should important contracts be put in writing, but they should also be made as clear, precise and complete as possible. Do not take it for granted that a legal phrase which you cannot fully understand is meaningless, for it may prove of great importance. Do not accept the other party's explanation of it, but take independent advice. Do not spare pains in providing for all dangerous contingencies that may have any bearing on the carrying out of the contract. After a contract is signed, never alter it unless all parties consent in writing.

CHAPTER XII.

RULES FOR THE CONSTRUCTION OF CONTRACTS.

When a contract has been proved in court, the decision of any controversy between the parties will involve either some disputed question of law or some dispute as to a matter of fact, or both. Usually the judges decide points of law, and leave disputes of fact for the decision of a jury. When the parties contradict each other as to the terms of a verbal agreement, the judge who hears the case will instruct the jury about the law involved, and then the jury will give a verdict either for the plaintiff or the defendant. Where there is no dispute as to the terms of the agreement, the courts will try to gather the intention of the parties from the words that were used. Since a contract is essentially an agreement, no judge would enforce it according to the literal meaning of the words used if a closer inspection of the contract would clearly reveal that the parties had an entirely different understanding of it. While a judge will not slavishly follow the expressions used by the parties, if to do so would defeat their prevailing intention, yet, in the case of a written contract, every word and phrase is given weight in getting at that intention. The courts do not like to admit verbal testimony to explain a

written contract, except as a last resort, for the parties are supposed to have embodied their agreement in the writing. See *Rinker v. Aetna Life Insurance Co.* (1906), 214 Pa. 608.

In the interpretation of a contract, the plain, simple meaning of words is given to them, unless it appears that they were used in some technical or extraordinary way. Again, the courts consider that the parties probably intended to make a sensible agreement in accordance with law, and any construction which would make it look absurd or illegal will be avoided if fairly possible. Agreements will be interpreted in the light of the circumstances surrounding the parties who made them. Proof of business customs often removes doubt as to what the parties intended. Where there is hopeless contradiction between two clauses in the same contract, which has been made on a printed form, and one of these clauses was printed in the form, while the other was written, the latter will prevail. It is reasonable to suppose that the intention of the parties was clearly directed to the written clause, while the printed one may have escaped their notice.

PART IV

THE DISCHARGE OF CONTRACTS

CHAPTER XIII.

DISCHARGE OF CONTRACTS BY AGREEMENT.

We have seen how a contract is formed, upon whom it operates, and also how it is interpreted by the courts. Finally, we ask about the methods in which it may be brought to an end. There are five methods by which a contract may be discharged or terminated. First, it may be discharged in the same way that it was formed, by agreement of the parties. Second, it may be discharged by performance. If all the parties have fully received what they were to get under it, and carried out what they were to do, the contract ceases to bind them, and passes out of existence. Third, it may be discharged by breach. If one party breaks the contract, the other is no longer bound to go ahead with it, but may treat it as discharged, and sue to recover whatever damages he has suffered. Fourth, it may be discharged in a few rare cases by occurrences which make performance impossible. Fifth, one of the parties may obtain a discharge in bankruptcy, which usually entails the discharge of almost all the contracts to which the bankrupt is a party. This chapter deals with the first method of discharging a contract.

(A) BY CONTRACT OF RELEASE.

The parties to a contract are free either to make it or not to make it, but they are bound by it as soon as it is made. One cannot drop it without the other's consent. There is no reason, however, to forbid the termination of it at any time, provided all the parties are willing. Under the seventh rule

about consideration, we saw that before the completion of a contract, the parties may by a second contract change the terms of the first one. Instead of substituting a new contract for the old, the parties may agree merely to cancel the old one entirely. If, when the cancellation agreement is made, neither party has completed his part of the contract, the release of one from the obligation to fulfil what he is bound to do is consideration for the release of the other from a similar obligation. If, on the contrary, one party has already completed what he is to do, and agrees to forgive the other party without any consideration, this agreement should be under seal. The agreement to discharge a contract should itself contain the elements necessary for the formation of a perfect contract, including seal or consideration. A reference to what is said under the seventh rule about consideration will make this point clearer.

(B) BY CONTRACT OF NOVATION.

Under the seventh rule just mentioned, something was said about a novation, which is a new contract superseding an old one. Where the parties to a contract make a new contract about the same matter, which is inconsistent with the old one, it may be inferred that they intend to drop the old one, even though they do not expressly say so. An agreement of novation, therefore, discharges the old contract.

(C) BY THE OPERATION OF A CONDITION SUBSEQUENT IN THE ORIGINAL CONTRACT ITSELF.

When a contract provides that it may be set aside upon a certain condition, the fulfilment of this condition will discharge it. For instance, suppose you buy goods at a store which allows its customers to return such goods within ten days. The contract of purchase which you make is subject to the condition subsequent permitting you to set it aside if you exercise your privilege of returning the goods. Many bonds,

which are for the most part sealed contracts for the payment of money, are made with a condition subsequent. For instance, in the case of many bail bonds, the contract commences with an absolute promise to pay a certain sum to the Commonwealth of Pennsylvania, but a condition provides that the bond shall be void if the person who is accused of crime will subsequently present himself for trial at the proper time.

CHAPTER XIV.

DISCHARGE OF CONTRACTS BY PERFORMANCE.

It is obvious that a contract is terminated when everything required by it has been fully accomplished. Sometimes, in the case of a sale contract, the purchaser when asked to pay will offer his own or a third party's promissory note for the amount due, instead of cash. If the note is not paid, the seller may sue either on the note or on the original claim to cover which it was given. His acceptance of the note is regarded merely as a conditional payment. One who owes several debts to the same party may direct the application of any payment. If he does not do so, the creditor may apply it to any debt. If neither applies it, the court may apply it to the oldest or least secured debt.

When a party is willing and able to perform what he is to do under the terms of a contract, but the other party refuses to accept performance, the former should guard against the possibility of future litigation by preserving evidence to show that he was not to blame. He should usually make what is called a "tender," which is a definite offer or attempt to perform.

If the debtor owes, say \$1,000, and takes that sum in gold, treasury notes or silver dollars to the creditor, who refuses to accept it, the debtor has done his part. If the creditor sues him afterwards, judgment for \$1,000 may be recovered against the debtor, but not for costs of suit or interest for the interval between the tender and the date of judgment. Where tender is to be made, not of money due, but

of the performance of some other contractual obligation, the form of tender varies widely with the circumstances of the case. If a man has agreed, for instance, to buy a heavy machine, and gives notice after it is manufactured for him that he will not take it, it is unnecessary for the seller to transport the machine to the buyer's place of business, in order to make a legal tender of performance.

In the course of performing a large building or engineering contract, it usually happens that there are at least some trifling defects in materials or workmanship. If these defects have been caused by no desire on the contractor's part to cheat the other party, the doctrine of substantial performance protects him. This is to be seen from the case of *Chambers v. Jaynes* (1846), 4 Pa. 39. Chambers agreed to build two houses for Jaynes. When he sued for the purchase money, Jaynes defended on the ground that a second coat of paint had not been put on a few doors and shutters, and that there was no glass in one of the cellar windows. These omissions could be supplied for \$10. The court held that where a party has substantially and in good faith complied with his contract, he cannot be deprived of compensation on account of some slight imperfection for which the other party may be recompensed by an allowance of money. Such allowance will be granted, as a set-off or deduction.

Sometimes an agreement provides that one party must complete performance in a manner satisfactory to the other, or to the other's engineer or architect. You should beware of agreeing to put yourself thus at the other party's mercy. In the case of *Boiler Works v. Schnader* (1893), 155 Pa. 394, it was proved that Schnader bought a heater, under a contract which contained the following clause: "We guarantee this apparatus to give entire satisfaction in its operation, and should it prove unsatisfactory after a thorough and reasonable trial we will remove it at our expense." Schnader died four days after the heater was installed in his house without having expressed any opinion about it. His executor, to whom the house was willed, lived there, and the heater was unsatisfactory to him from the day that it was first started. He gave it a

thorough trial, and the court allowed him to reject it. The court stated that the heater was not a piece of machinery designed to accomplish some single purpose in which power and durability alone constitute satisfactoriness. A sawmill may be warranted as of a capacity to cut a certain quantity of lumber per day; a locomotive may be warranted to draw a certain number of tons; and if there be a guaranty that the purchaser shall be satisfied, it can be reasonably presumed that the specified power was all that the parties intended. When, however, the subject of the contract is household furniture, or a suit of clothes, or a work of art, the question is not whether the thing contracted for had a certain strength or a particular dimension as specified in the contract, but there come in to make up satisfaction or dissatisfaction those qualities which please, or those defects which are nothing more than annoying. If the heater was a source of vexation to Schnader's executor, instead of a satisfaction, he was not bound to keep and pay for it. If it could be proved that his dissatisfaction was not genuine and expressed in good faith, the executor could have been held liable, for he would not be allowed to reject it out of mere caprice or dishonesty, or without a fair test of its qualities. See also *Payne v. Roberts* (1906), 214 Pa. 568.

CHAPTER XV.

DISCHARGE OF CONTRACTS BY BREACH.

If one party fails to perform, in an essential matter, what he is bound to do under the contract, the other party may treat the contract as broken, and refuse to go ahead with it himself. Not every breach of a contract will discharge it, and a distinction must be drawn between terms which are of vital importance, and those which are merely collateral.

When the contract fixes a certain *time* by which performance must be completed, the question is frequently raised whether the time clause is essential or not. In mercantile contracts, if one party delays performance beyond the date

agreed upon, the other may generally refuse to accept tardy performance and may drop the matter or make arrangements elsewhere. If, however, by his words or conduct he gives the delinquent party to understand that he will not insist on prompt performance, he thereby waives the time clause. In most building contracts a time clause is not regarded as vital, unless the building in question is to be erected for a temporary purpose. If an exposition building is to be erected for a fair, it would be absurd for the builder to demand payment should he fail to erect it until the fair is almost over. Instead of receiving money from the other party, the builder would probably have to pay him damages. Even where a building is for permanent use, the builder who fails to complete it on time must compensate the owner for damages caused by the delay. In that case, while the breach does not justify the owner in declaring the entire contract discharged, it will, nevertheless, enable him to deduct from any payment which he makes to the builder whatever damages he has suffered as a natural consequence of the delay. If he has foolishly paid the builder beforehand, he may sue for the damages. To forestall the trouble of proving exactly what damages are caused by a delay, the parties sometimes provide in their original agreement that a certain sum shall be paid as liquidated damages by the builder for each day that he may take to complete his work after the time fixed. The phrase "*liquidated damages*" means that the parties agree to consider the damages as ascertained, without itemized proof as to what they consist of, or how they were caused.

The courts will not enforce a provision respecting liquidated damages, if it seems highly unreasonable. While contracts are usually enforced in all their terms, yet the judges do not like to permit one who has broken a contract to be unduly punished. It is entirely proper that he should be made to pay damages to the injured party, but when the sum agreed upon is clearly in the nature of a penalty, the situation is different. Where the same figure is agreed upon as liquidated damages in the event of different kinds of breaches, some important and some trifling, it looks as if no proportion were

observed between the breach and the damages supposed to flow from it, and the courts are disposed to disregard the entire clause on the ground that it imposes an unreasonable penalty. On the other hand, the courts are quick to find a good reason for upholding a clause regarding liquidated damages. For instance, if a building is to be completed by May 1, 1906, and the builder is to pay \$30 as liquidated damages for each day's delay, the courts are more disposed to uphold this term, if it is further agreed that the builder shall get, say, \$25 for each day saved in case he completes ahead of time.

As soon as one party learns of the other's breach of contract, he should take measures to keep the resulting loss down as much as possible. For instance, if a teamster is employed to do hauling for a year, but is unjustly discharged during the year, he should seek other work for his teams, and not let them stand in his stable with the hope of recovering the entire contract price from his employer. He cannot recover any damages beyond such as he clearly proves. Only the net profits of a contract can be recovered, and when the injured party asks damages for these profits, he must show that they are such as the other party could reasonably have foreseen. The case of *Emig v. Spatz* (1893), 155 Pa. 642, shows that the courts will not usually allow an injured party to recover greater damages than he has actually suffered. Clayton E. Emig & Co. agreed to drill certain wells for Spatz for \$500. They sent men and machinery to the place where the wells were to be sunk, but Spatz refused to permit the work to be done. Emig & Co. wanted to recover the entire sum of \$500, but the court made them deduct the amount of money which they had saved by not completing performance. This deduction covered the value of materials which they were spared from buying, and also the wages which the notice given by Spatz saved them from having to pay. If Spatz had permitted them without objection to complete the work, and then broken it by refusing to pay them, their pecuniary loss, under the contract, as caused by the breach, would be \$500. Since Spatz had prevented them from incurring certain expenditures by declining to let them go ahead with the work, their loss was reduced by so much.

If X who has agreed to sell you a certain article fails to deliver it, you can make him pay only your net loss. This loss consists of the difference between the price at which X was to sell it, and the market price of such articles at the time and place of delivery, together with interest on this amount of difference. The mere fact that the non-delivery prevented you from selling the article at a big advance to a customer, does not entitle you to recover the profits you would have made on this second transaction, unless the second transaction was clearly contemplated by you and X at the time of your original agreement.

Returning to the distinction between essential and non-essential terms of contract, we may state the rule to be that the intention of the parties is followed by the courts. The parties may declare in their agreement that the literal fulfilment of some term, seemingly of scant importance, is an absolute condition of the contract. If they did not give this term the importance of a *condition*, the courts would hold it only a *collateral warranty*. A condition is an essential term, the breach of which enables the injured party to treat the contract as ended. A collateral warranty is a non-essential term, the breach of which does not discharge the contract, but merely gives the injured party a right to damages. In the absence of an express statement from the parties themselves, a judge will be guided by the surrounding circumstances in rendering his decision. If a man were employed to instruct a company of actors, his failure to appear at, say, the first two rehearsals, would justify the manager in discharging him, and employing somebody else. On the contrary, if one of the actors who had a monologue part were absent from these rehearsals, his contract would probably not be discharged. The instructor was engaged solely for the rehearsals, but attendance at them is only an incidental part of the actor's employment. If the actor remains away from a few rehearsals, and it appears that his preparation for the stage is not thereby marred, the contract is not discharged, unless it specifically provides that attendance at rehearsals shall be an absolute condition.

The question as to whether or not a breach of contract is

sufficiently important to discharge it, sometimes comes up in a contract which relates to several different matters, or which is to be performed in several instalments. If performance is entirely deficient as to part of such a contract, it is often doubtful whether the contract is discharged partially or wholly. If the contract is *one entire contract*, it is wholly discharged. It is only partially discharged if it is *a severable contract*. A severable contract is really a number of different contracts.

If what is to be performed by you under a contract consists of several distinct items, and the consideration to be furnished by the other party is apportioned to each item of your performance, such a contract is usually severable. The mere fact that your performance is split up into different parts, and that the consideration is split up into the same number of parts does not make the contract severable unless each item of consideration is intended to correspond with a certain item of performance. Again, the mere fact that the subject matter of the contract is sold by quantity or weight will not justify the seller in performing only partly, and demanding payment calculated according to the quantity or weight of what he has actually delivered. Again, where you purchase several articles from the same seller at an auction sale, the contract is entire, although the articles are bought on different bids and the price of each article has no bearing on that of the others.

Where it clearly appears that it would defeat the real intention of the parties to enforce any of the foregoing rules, the courts are disposed to abandon them. In the case of *Reybold v. Voorhees* (1858), 30 Pa. 116, a contract was held entire, even though performance was to be made in a number of instalments, and the consideration was apportioned to each week's instalments. Reybold agreed to sell all the peaches growing on his Delaware farms to Voorhees, Marlatt & Co. at 75 cents per basket; payments to be made at the end of each week. Reybold began delivering peaches the same week that the contract was made, but was requested to take them back until the following Monday. He did so, and delivered peaches all the following week, and the first day of the next week, when he stopped because he had not been paid for the

first week's delivery. A few days later Voorhees, Marlatt & Co. offered to pay what they owed him, and tried to induce him to continue delivery. Failing in this, they sued him, but the court held that he was justified in dropping the entire contract. While the same degree of punctuality might not be exacted from the purchaser of, for instance, hardware, the court stated that promptness is of essential importance in the execution of a contract for the sale of a ripening crop of peaches. Not receiving payment for the first week's instalment, Reybold had a right to treat the entire contract as discharged.

The party who is injured by the breach of a contract may recover damages from the other. If it is necessary to bring suit to get these damages, it may take months or years before judgment is finally rendered. Even when he gets the judgment, he will find that it does not include an allowance for what he has paid his lawyer or for the annoyance incident to a lawsuit. It is often better, therefore, especially in building and engineering contracts, to provide that in the event of a breach, *arbitrators* shall be appointed to determine the extent of the damages caused by it. One arbitrator may be chosen by each party, and if there are only two parties, the two arbitrators may select a third. An arbitration clause is of use in enabling disputes of all kinds to be speedily settled.

After the commission of a breach by one party to a contract, the other has six years within which to start suit. In case a sealed contract is broken, the injured party has twenty years. It is always safer to start proceedings promptly, for circumstances may intervene to prejudice the rights of the injured party. Even though the injured party does not intend to bring suit at once to recover damages for a breach, he should usually notify the other that he is not satisfied with performance, especially where the other is continuing to perform the contract in the same unsatisfactory way. If he knows, for instance, that the other party has turned over the work of performance to a third person, in violation of the contract, and continues without complaint to let this third person complete it, he cannot object long afterwards. Even the breach

of absolute conditions may be waived by the injured party, if he acquiesces in them, and lets the other party complete performance in continued violation of the conditions. The injured party may, however, usually demand an allowance for a breach of condition, although he has failed to utilize it as a means of setting the entire contract aside.

CHAPTER XVI.

DISCHARGE OF CONTRACTS BY IMPOSSIBILITY.

In most cases it is no excuse for a party who cannot fulfil his contractual promise to prove that performance is impossible. He should have learned that before making the promise. Still more, it is no excuse for him to say that the performance of what he has agreed to do would entail heavy expense, inconvenience and hardship, beyond his expectation. In a few rare cases, however, impossibility has been held to discharge a contract.

In the case of *Lovering v. Coal Co.* (1867), 54 Pa. 291, it appeared that the coal company had agreed with Lovering and others to deliver 4,000 tons of Buck Mountain egg coal. Shortly afterwards a terrible flood swept away a great part of the transportation line of the Lehigh Coal and Navigation Co., which both parties had known to be an indispensable means of bringing the coal to the place of delivery. The court held that while this link in the chain of transportation continued broken, the coal company was excused from fulfilling the contract, but no longer. If an ordinary spring freshet had prevented delivery, the coal company would have been liable to pay damages, because such things should be foreseen. Thus, if a builder agrees to finish his work by a certain day, he cannot justify a delay on the mere ground that the weather is severe, and prevents prompt completion.

Where the contract is for purely personal services, it is discharged if performance is prevented by the death or sickness of the person who is to render them. The majority of

contracts, however, survive the death of one or both of the parties. The rights created by such a contract pass to the estate of the party who possesses them, while the obligations figure as liabilities of the estate.

CHAPTER XVII.

DISCHARGE OF CONTRACTS BY BANKRUPTCY.

Only the United States Congress has power to pass a bankruptcy law to discharge insolvent debtors from the burden of their debts and other contractual obligations. The bankruptcy system established by Congress in 1898 was designed not only to relieve poor debtors and enable them to start life anew, but also to prevent one creditor from obtaining an improper preference over the others. Bankruptcy proceedings may, therefore, be started not only by an insolvent, but also by creditors, and the entire act aims at adjusting the rights of all parties interested.

Although the Bankrupt Act is in force throughout all the states, it allows a Pennsylvania bankrupt the same *exemption* as our state laws prescribe. This is regulated by the act of April 9, 1849, and supplements, which enable one whose goods are being sold by the sheriff on any judgment for a breach of contract, or whose goods are seized for arrears of rent, to retain property to the value of \$300, in addition to all wearing apparel of the debtor and his family, and all sewing machines, Bibles and school-books in use by them.

The sixty-fourth section of the Bankrupt Act gives a certain priority to debts owing to any person who by the laws of the states or of the United States is entitled thereto. This gives landlords in Pennsylvania a certain preference for **one** year's rent out of the sale of such goods upon the leased premises as are subject to seizure for arrears of rent. The subject of real estate leases will be considered in the third book.

The sixty-fourth section of the Bankrupt Act gives a certain priority to claims for wages, not to exceed \$300 for

each claimant, earned by workmen, clerks and servants within three months before the commencement of bankruptcy proceedings. The priority obtained by wage claimants is not allowed to affect the lien of the ordinary mortgage, which is superior even to the bankrupt's claim for exemption. Creditors of bankrupt estates often find it to their advantage to scrutinize all claims for which priority of payment is demanded, for many such claims can be defeated, which, if allowed, will prevent the ordinary creditors from getting good dividends.

When you learn that one of your debtors has gone into bankruptcy, you should take prompt measures to prove your claim, if you want to get a share of his assets. You must prove it according to a set form, printed copies of which may be bought from any law stationer. There are different forms for secured and unsecured creditors, and the form for proof by a partnership is slightly different from that made by an individual creditor, or a corporation. The treasurer of a corporation is the proper officer to swear to its claim. If your corporation employs no official called the treasurer, the person whose duties are most nearly like those of a treasurer is the proper one. For instance, the cashier of a national bank swears to the bank's proof of claim.

If you claim on a bill for merchandise, a full, itemized account should be attached to your sworn proof. If you claim on a promissory note, bond or other written contract, you should take the original document and a copy of it to the referee in bankruptcy. He will compare the two, and file the copy with your sworn proof of claim, so that you may safely preserve the original yourself. Usually you have a year within which to file your claim, but, if possible, prove it before the referee several days in advance of the first meeting of the bankrupt's creditors. This gives you a chance to correct your proof if it is in unsatisfactory shape, and thus to qualify yourself to vote for a good trustee. It is often wise to give your attorney written authority to vote for you at creditors' meetings, especially at the first one when the trustee is elected. See that an honest, energetic trustee is chosen. Many a bankrupt estate which pays meagre dividends would yield the creditors much

more, if the trustee and his lawyer were less eager for their own enrichment, and willing to work hard for the benefit of the estate.

The Bankrupt Act of July 1, 1898, as amended February 5, 1903, is fully set forth in the following paragraphs:

(A) THE UNITED STATES BANKRUPTCY ACT.

DIVISION FIRST.

Definitions.

SECTION 1. *Meaning of words and phrases.*—(a) The words and phrases used in this act and in proceedings pursuant hereto shall, unless the same be inconsistent with the context, be construed as follows: (1) "A person against whom a petition has been filed" shall include a person who has filed a voluntary petition; (2) "adjudication" shall mean the date of the entry of a decree that the defendant, in a bankruptcy proceeding, is a bankrupt, or if such decree is appealed from, then the date when such decree is finally confirmed; (3) "appellate courts" shall include the circuit courts of appeals of the United States, the supreme courts of the Territories, and the Supreme Court of the United States; (4) "bankrupt" shall include a person against whom an involuntary petition or an application to set a composition aside or to revoke a discharge has been filed, or who has filed a voluntary petition, or who has been adjudged a bankrupt; (5) "clerk" shall mean the clerk of a court of bankruptcy; (6) "corporations" shall mean all bodies having any of the powers and privileges of private corporations not possessed by individuals or partnerships, and shall include limited or other partnership associations organized under laws making the capital subscribed alone responsible for the debts of the association; (7) "court" shall mean the court of bankruptcy in which the proceedings are pending, and may include the referee; (8) "courts of bankruptcy" shall include the district courts of the United States and of the Territories, the supreme

court of the District of Columbia, and the United States court of the Indian Territory, and of Alaska; (9) "creditor" shall include anyone who owns a demand or claim provable in bankruptcy, and may include his duly authorized agent, attorney, or proxy; (10) "date of bankruptcy," or "time of bankruptcy," or "commencement of proceedings," or "bankruptcy," with reference to time, shall mean the date when the petition was filed; (11) "debt" shall include any debt, demand, or claim provable in bankruptcy; (12) "discharge" shall mean the release of a bankrupt from all of his debts which are provable in bankruptcy, except such as are excepted by this act; (13) "document" shall include any book, deed, or instrument in writing; (14) "holiday" shall include Christmas, the Fourth of July, the Twenty-second of February, and any day appointed by the President of the United States or the Congress of the United States as a holiday or as a day of public fasting or thanksgiving; (15) a person shall be deemed insolvent within the provisions of this act whenever the aggregate of his property, exclusive of any property which he may have conveyed, transferred, concealed, or removed, or permitted to be concealed or removed, with intent to defraud, hinder or delay his creditors, shall not, at a fair valuation, be sufficient in amount to pay his debts; (16) "judge" shall mean a judge of a court of bankruptcy, not including the referee; (17) "oath" shall include affirmation; (18) "officer" shall include clerk, marshal, receiver, referee, and trustee, and the imposing of a duty upon or the forbidding of an act by any officer shall include his successor and any person authorized by law to perform the duties of such officer; (19) "persons" shall include corporations, except where otherwise specified, and officers, partnerships, and women, and when used with reference to the commission of acts which are herein forbidden shall include persons who are participants in the forbidden acts, and the agents, officers, and members of the board of directors or trustees, or other similar controlling bodies of corporations; (20) "petition" shall mean a paper filed in a court of bankruptcy or with a clerk or deputy clerk by a debtor praying for the benefits of this act, or by creditors alleging the commission

of an act of bankruptcy by a debtor therein named; (21) "referee" shall mean the referee who has jurisdiction of the case or to whom the case has been referred, or anyone acting in his stead; (22) "conceal" shall include secrete, falsify, and mutilate; (23) "secured creditor" shall include a creditor who has security for his debt upon the property of the bankrupt of a nature to be assignable under this act, or who owns such a debt for which some indorser, surety, or other persons secondarily liable for the bankrupt has such security upon the bankrupt's assets; (24) "States" shall include the Territories, the Indian Territory, Alaska, and the District of Columbia; (25) "transfer" shall include the sale and every other and different mode of disposing of or parting with property, or the possession of property, absolutely or conditionally, as a payment, pledge, mortgage, gift, or security; (26) "trustee" shall include all of the trustees of an estate; (27) "wage-earner" shall mean an individual who works for wages, salary, or hire, at a rate of compensation not exceeding one thousand five hundred dollars per year; (28) words importing the masculine gender may be applied to and include corporations, partnerships, and women; (29) words importing the plural number may be applied to and mean only a single person or thing; (30) words importing the singular number may be applied to and mean several persons or things.

DIVISION SECOND.

Creation of courts of bankruptcy and their jurisdiction.

SECTION 2. That the courts of bankruptcy as hereinbefore defined, viz., the district courts of the United States in the several States, the supreme court of the District of Columbia, the district courts of the several Territories, and the United States courts in the Indian Territory and the District of Alaska, are hereby made courts of bankruptcy, and are hereby invested, within their respective territorial limits as now established, or as they may be hereafter changed, with such jurisdiction at law and in equity as will enable them to

exercise original jurisdiction in bankruptcy proceedings, in vacation in chambers and during their respective terms, as they are now or may be hereafter held, to (1) adjudge persons bankrupt who have had their principal place of business, resided, or had their domicile within their respective territorial jurisdictions for the preceding six months, or the greater portion thereof, or who do not have their principal place of business, reside, or have their domicile within the United States, but have property within their jurisdictions, or who have been adjudged bankrupts by courts of competent jurisdiction without the United States and have property within their jurisdiction; (2) allow claims, disallow claims, reconsider allowed or disallowed claims, and allow or disallow them against bankrupt estates; (3) appoint receivers or the marshals, upon application of parties in interest, in case the courts shall find it absolutely necessary, for the preservation of estates, to take charge of the property of bankrupts after the filing of the petition and until it is dismissed or the trustee is qualified; (4) arraign, try, and punish bankrupts, officers, and other persons, and the agents, officers, members of the board of directors or trustees, or other similar controlling bodies of corporations for violations of this act, in accordance with the laws of procedure of the United States now in force, or such as may be hereafter enacted, regulating trials for the alleged violation of laws of the United States; (5) authorize the business of bankrupts to be conducted for limited periods by receivers, the marshals, or trustees, if necessary in the best interests of the estates, and allow such officers additional compensation for such services, but not at a greater rate than in this act allowed trustees for similar services; (6) bring in and substitute additional persons or parties in proceedings in bankruptcy when necessary for the complete determination of a matter in controversy; (7) cause the estates of bankrupts to be collected, reduced to money and distributed, and determine controversies in relation thereto, except as herein otherwise provided; (8) close estates, whenever it appears that they have been fully administered, by approving the final accounts and discharging the trustees, and reopen them whenever it

appears they were closed before being fully administered; (9) confirm or reject compositions between debtors and their creditors, and set aside compositions and reinstate the cases; (10) consider and confirm, modify or overrule, or return, with instructions for further proceedings, records and findings certified to them by referees; (11) determine all claims of bankrupts to their exemptions; (12) discharge or refuse to discharge bankrupts and set aside discharges and reinstate the cases; (13) enforce obedience by bankrupts, officers, and other persons to all lawful orders, by fine or imprisonment or fine and imprisonment; (14) extradite bankrupts from their respective districts to other districts; (15) make such orders, issue such process, and enter such judgments in addition to those specifically provided for as may be necessary for the enforcement of the provisions of this act; (16) punish persons for contempts committed before referees; (17) pursuant to the recommendation of creditors, or when they neglect to recommend the appointment of trustees, appoint trustees, and upon complaints of creditors, remove trustees for cause upon hearings and after notices to them; (18) tax costs, whenever they are allowed by law, and render judgments therefor against the unsuccessful party, or the successful party for cause, or in part against each of the parties, and against estates, in proceedings in bankruptcy; and (19) transfer cases to other courts of bankruptcy.

Nothing in this section contained shall be construed to deprive a court of bankruptcy of any power it would possess were certain specific powers not herein enumerated.

DIVISION THIRD.

Bankrupts.

SECTION 3. *Acts of bankruptcy.*—(a) Acts of bankruptcy by a person shall consist of his having (1) conveyed, transferred, concealed, or removed, or permitted to be concealed or removed, any part of his property with intent to hinder, delay, or defraud his creditors, or any of them; or (2) transferred,

while insolvent, any portion of his property to one or more of his creditors with intent to prefer such creditors over his other creditors; or (3) suffered or permitted, while insolvent, any creditor to obtain a preference through legal proceedings, and not having at least five days before a sale or final disposition of any property affected by such preference vacated or discharged such preference; or (4) made a general assignment for the benefit of his creditors, or, being insolvent, applied for a receiver or trustee for his property or because of insolvency a receiver or trustee has been put in charge of his property under the laws of a State, of a Territory, or of the United States; or (5) admitted in writing his inability to pay his debts and his willingness to be adjudged a bankrupt on that ground.

(b) A petition may be filed against a person who is insolvent and who has committed an act of bankruptcy within four months after the commission of such act. Such time shall not expire until four months after (1) the date of the recording or registering of the transfer or assignment when the act consists in having made a transfer of any of his property with intent to hinder, delay, or defraud his creditors or for the purpose of giving a preference as hereinbefore provided, or a general assignment for the benefit of his creditors, if by law such recording or registering is required or permitted, or, if it is not, from the date when the beneficiary takes notorious, exclusive, or continuous possession of the property unless the petitioning creditors have received actual notice of such transfer or assignment.

now (c) It shall be a complete defense to any proceedings in bankruptcy instituted under the first subdivision of this section to allege and prove that the party proceeded against was not insolvent as defined in this act at the time of the filing the petition against him, and if solvency at such date is proved by the alleged bankrupt the proceedings shall be dismissed, and under said subdivision one the burden of proving solvency shall be on the alleged bankrupt.

(d) Whenever a person against whom a petition has been filed as hereinbefore provided under the second and third subdivisions of this section takes issue with and denies the allega-

tion of his insolvency, it shall be his duty to appear in court on the hearing, with his books, papers, and accounts, and submit to an examination, and give testimony as to all matters tending to establish solvency or insolvency, and in case of his failure to so attend and submit to examination the burden of proving his solvency shall rest upon him.

(e) Whenever a petition is filed by any person for the purpose of having another adjudged a bankrupt, and an application is made to take charge of and hold the property of the alleged bankrupt, or any part of the same, prior to the adjudication and pending a hearing on the petition, the petitioner or applicant shall file in the same court a bond with at least two good and sufficient sureties who shall reside within the jurisdiction of said court, to be approved by the court or a judge thereof, in such sum as the court shall direct, conditioned for the payment, in case such petition is dismissed, to the respondent, his or her personal representatives, all costs, expenses, and damages occasioned by such seizure, taking, and detention of the property of the alleged bankrupt.

If such petition be dismissed by the court or withdrawn by the petitioner, the respondent or respondents shall be allowed all costs, counsel fees, expenses, and damages occasioned by such seizure, taking, or detention of such property. Counsel fees, costs, expenses, and damages shall be fixed and allowed by the court, and paid by the obligors in such bond.

SECTION 4. *Who may become bankrupts.*—(a) Any person who owes debts, except a corporation, shall be entitled to the benefits of this act as a voluntary bankrupt.

(b) Any natural person, except a wage-earner, or a person engaged chiefly in farming or the tillage of the soil, any unincorporated company, and any corporation engaged principally in manufacturing, trading, printing, publishing, mining, or mercantile pursuits, owing debts to the amount of one thousand dollars or over, may be adjudged an involuntary bankrupt upon default or an impartial trial, and shall be subject to the provisions and entitled to the benefits of this act. Private bankers, but not national banks or banks incorporated under State or Territorial laws, may be adjudged involuntary bank-

rupts. The bankruptcy of a corporation shall not release its officers, directors, or stockholders, as such, from any liability under the laws of a State or Territory or of the United States.

† SECTION 5. *Partners.*—(a) A partnership, during the continuation of the partnership business, or after its dissolution and before the final settlement thereof, may be adjudged a bankrupt.

(b) The creditors of the partnership shall appoint the trustee; in other respects so far as possible the estate shall be administered as herein provided for other estates.

(c) The court of bankruptcy which has jurisdiction of one of the partners may have jurisdiction of all the partners and of the administration of the partnership and individual property.

(d) The trustee shall keep separate accounts of the partnership property and of the property belonging to the individual partners.

(e) The expenses shall be paid from the partnership property and the individual property in such proportions as the court shall determine.

(f) The net proceeds of the partnership property shall be appropriated to the payment of the partnership debts, and the net proceeds of the individual estate of each partner to the payment of his individual debts. Should any surplus remain of the property of any partner after paying his individual debts, such surplus shall be added to the partnership assets and be applied to the payment of the partnership debts. Should any surplus of the partnership property remain after paying the partnership debts, such surplus shall be added to the assets of the individual partners in the proportion of their respective interests in the partnership.

(g) The court may permit the proof of the claim of the partnership estate against the individual estates, and vice versa, and may marshal the assets of the partnership estate and individual estates so as to prevent preferences and secure the equitable distribution of the property of the several estates.

(h) In the event of one or more but not all of the members of a partnership being adjudged bankrupt, the partnership

property shall not be administered in bankruptcy, unless by consent of the partner or partners not adjudged bankrupt; but such partner or partners not adjudged bankrupt shall settle the partnership business as expeditiously as its nature will permit, and account for the interest of the partner or partners adjudged bankrupt.

SECTION 6. *Exemptions of bankrupts.*—(a) This act shall not affect the allowance to bankrupts of the exemptions which are prescribed by the State laws in force at the time of the filing of the petition in the State wherein they have had their domicile for the six months or the greater portion thereof immediately preceding the filing of the petition.

SECTION 7. *Duties of bankrupts.*—(a) The bankrupt shall (1) attend the first meeting of his creditors, if directed by the court or a judge thereof to do so, and the hearing upon his application for a discharge, if filed; (2) comply with all lawful orders of the court; (3) examine the correctness of all proofs of claims filed against his estate; (4) execute and deliver such papers as shall be ordered by the court; (5) execute to his trustee transfers of all his property in foreign countries; (6) immediately inform his trustee of any attempt, by his creditors or other persons, to evade the provisions of this act, coming to his knowledge; (7) in case of any person having to his knowledge proved a false claim against his estate, disclose that fact immediately to his trustee; (8) prepare, make oath to, and file in court within ten days, unless further time is granted, after the adjudication, if an involuntary bankrupt, and with the petition if a voluntary bankrupt, a schedule of his property, showing the amount and kind of property, the location thereof, its money value in detail, and a list of his creditors, showing their residences, if known, if unknown, that fact to be stated, the amounts due each of them, the consideration thereof, the security held by them, if any, and a claim for such exemptions as he may be entitled to, all in triplicate, one copy of each for the clerk, one for the referee, and one for the trustee; and (9) when present at the first meeting of his creditors, and at such other times as the court shall order, submit to an examination concerning the conducting of his business, the cause of his

bankruptcy, his dealings with his creditors and other persons, the amount, kind, and whereabouts of his property, and, in addition, all matters which may affect the administration and settlement of his estate; but no testimony given by him shall be offered in evidence against him in any criminal proceeding.

Provided, however, That he shall not be required to attend a meeting of his creditors, or at or for an examination at a place more than one hundred and fifty miles distant from his home or principal place of business, or to examine claims except when presented to him, unless ordered by the court, or a judge thereof, for cause shown, and the bankrupt shall be paid his actual expenses from the estate when examined or required to attend at any place other than the city, town, or village of his residence.

SECTION 8. *Death or insanity of bankrupts.*—(a) The death or insanity of a bankrupt shall not abate the proceedings, but the same shall be conducted and concluded in the same manner, so far as possible, as though he had not died or become insane: Provided, That in case of death the widow and children shall be entitled to all rights of dower and allowance fixed by the laws of the State of the bankrupt's residence.

SECTION 9. *Protection and detention of bankrupts.*—(a) A bankrupt shall be exempt from arrest upon civil process except in the following cases: (1) When issued from a court of bankruptcy for contempt or disobedience of its lawful orders; (2) when issued from a State court having jurisdiction, and served within such State, upon a debt or claim from which his discharge in bankruptcy would not be a release, and in such case he shall be exempt from such arrest when in attendance upon a court of bankruptcy or engaged in the performance of a duty imposed by this act.

(b) The judge may, at any time after the filing of a petition by or against a person, and before the expiration of one month after the qualification of the trustee, upon satisfactory proof by the affidavits of at least two persons that such bankrupt is about to leave the district in which he resides or has his principal place of business to avoid examination, and that his departure will defeat the proceedings in bankruptcy, issue a

warrant to the marshal, directing him to bring such bankrupt forthwith before the court for examination. If upon hearing the evidence of the parties it shall appear to the court or a judge thereof that the allegations are true and that it is necessary, he shall order such marshal to keep such bankrupt in custody not exceeding ten days, but not imprison him, until he shall be examined and released or give bail conditioned for his appearance for examination, from time to time, not exceeding in all ten days, as required by the court, and for his obedience to all lawful orders made in reference thereto.

SECTION 10. *Extradition of bankrupts.*—(a) Whenever a warrant for the apprehension of a bankrupt shall have been issued, and he shall have been found within the jurisdiction of a court other than the one issuing the warrant, he may be extradited in the same manner in which persons under indictment are now extradited from one district within which a district court has jurisdiction to another.

SECTION 11. *Suits by and against bankrupts.*—(a) A suit which is founded upon a claim from which a discharge would be a release, and which is pending against a person at the time of the filing of a petition against him, shall be stayed until after an adjudication or the dismissal of the petition; if such person is adjudged a bankrupt, such action may be further stayed until twelve months after the date of such adjudication, or, if within that time such person applies for a discharge, then until the question of such discharge is determined.

(b) The court may order the trustee to enter his appearance and defend any pending suit against the bankrupt.

(c) A trustee may, with the approval of the court, be permitted to prosecute as trustee any suit commenced by the bankrupt prior to the adjudication, with like force and effect as though it had been commenced by him.

(d) Suits shall not be brought by or against a trustee of a bankrupt estate subsequent to two years after the estate has been closed.

SECTION 12. *Compositions, when confirmed.*—(a) A bankrupt may offer terms of composition to his creditors after, but not before, he has been examined in open court or at a meeting

of his creditors, and filed in court the schedule of his property and list of his creditors, required to be filed by bankrupts.

(b) An application for the confirmation of a composition may be filed in the court of bankruptcy after, but not before, it has been accepted in writing by a majority in number of all creditors whose claims have been allowed, which number must represent a majority in amount of such claims, and the consideration to be paid by the bankrupt to his creditors, and the money necessary to pay all debts which have priority and the cost of the proceedings, have been deposited in such place as shall be designated by and subject to the order of the judge.

(c) A date and place, with reference to the convenience of the parties in interest, shall be fixed for the hearing upon each application for the confirmation of a composition, and such objections as may be made to its confirmation.

(d) The judge shall confirm a composition if satisfied that (1) it is for the best interests of the creditors; (2) the bankrupt has not been guilty of any of the acts or failed to perform any of the duties which would be a bar to his discharge; and (3) the offer and its acceptance are in good faith and have not been made or procured except as herein provided, or by any means, promises, or acts herein forbidden.

(e) Upon the confirmation of a composition, the consideration shall be distributed as the judge shall direct, and the case dismissed. Whenever a composition is not confirmed, the estate shall be administered in bankruptcy as herein provided.

SECTION 13. *Compositions, when set aside.*—(a) The judge may, upon the application of parties in interest filed at any time within six months after a composition has been confirmed, set the same aside and reinstate the case if it shall be made to appear upon a trial that fraud was practiced in the procuring of such composition, and that the knowledge thereof has come to the petitioners since the confirmation of such composition.

SECTION 14. *Discharges, when granted.*—(a) Any person may, after the expiration of one month and within the next twelve months subsequent to being adjudged a bankrupt, file an application for a discharge in the court of bankruptcy in

which the proceedings are pending; if it shall be made to appear to the judge that the bankrupt was unavoidably prevented from filing it within such time, it may be filed within but not after the expiration of the next six months.

(b) The judge shall hear the application for a discharge, and such proofs and pleas as may be made in opposition thereto by parties in interest, at such time as will give parties in interest a reasonable opportunity to be fully heard, and investigate the merits of the application and discharge the applicant unless he has (1) committed an offense punishable by imprisonment as herein provided; or (2) with intent to conceal his financial condition, destroyed, concealed, or failed to keep books of account or records from which such condition might be ascertained; or (3) obtained property on credit from any person upon a materially false statement in writing made to such person for the purpose of obtaining such property on credit; or (4) at any time subsequent to the first day of the four months immediately preceding the filing of the petition transferred, removed, destroyed, or concealed, or permitted to be removed, destroyed, or concealed any of his property with intent to hinder, delay, or defraud his creditors; or (5) in voluntary proceedings been granted a discharge in bankruptcy within six years; or (6) in the course of the proceedings in bankruptcy refused to obey any lawful order of or to answer any material question approved by the court.

(c) The confirmation of a composition shall discharge the bankrupt from his debts, other than those agreed to be paid by the terms of the composition and those not affected by a discharge.

SECTION 15. *Discharges, when revoked.*—(a) The judge may, upon the application of parties in interest who have not been guilty of undue laches, filed at any time within one year after a discharge shall have been granted, revoke it upon a trial if it shall be made to appear that it was obtained through the fraud of the bankrupt, and that the knowledge of the fraud has come to the petitioners since the granting of the discharge, and that the actual facts did not warrant the discharge.

SECTION 16. *Co-debtors of bankrupts.*—(a) The liability

of a person who is a co-debtor with, or guarantor or in any manner a surety for, a bankrupt shall not be altered by the discharge of such bankrupt.

177 *SECTION 17. Debts not affected by a discharge.*—(a) A discharge in bankruptcy shall release a bankrupt from all of his provable debts, except such as (1) are due as a tax levied by the United States, the State, county, district, or municipality in which he resides; (2) are liabilities for obtaining property by false pretences or false representations, or for wilful and malicious injuries to the person or property of another, or for alimony due or to become due, or for maintenance or support of wife or child, or for seduction of an unmarried female, or for criminal conversation; (3) have not been duly scheduled in time for proof and allowance, with the name of the creditor if known to the bankrupt, unless such creditor had notice or actual knowledge of the proceedings in bankruptcy; or (4) were created by his fraud, embezzlement, misappropriation, or defalcation while acting as an officer or in any fiduciary capacity.

DIVISION FOURTH.

Courts and Procedure Therein.

SECTION 18. Process, pleadings, and adjudications.—

178 (a) Upon the filing of a petition for involuntary bankruptcy, service thereof, with a writ of subpœna, shall be made upon the person therein named as defendant in the same manner that service of such process is now had upon the commencement of a suit in equity in the courts of the United States, except that it shall be returnable within fifteen days, unless the judge shall for cause fix a longer time; but in case personal service cannot be made, then notice shall be given by publication in the same manner and for the same time as provided by law for notice by publication in suits to enforce a legal or equitable lien, in courts of the United States, except that, unless the judge shall otherwise direct, the order shall be published not more than once a week for two consecutive weeks, and the return day

shall be ten days after the last publication unless the judge shall for cause fix a longer time.

(b) The bankrupt, or any creditor, may appear and plead to the petition within five days after the return day, or within such further time as the court may allow.

(c) All pleadings setting up matters of fact shall be verified under oath.

(d) If the bankrupt, or any of his creditors, shall appear, within the time limited, and controvert the facts alleged in the petition, the judge shall determine, as soon as may be, the issues presented by the pleadings, without the intervention of a jury, except in cases where a jury trial is given by this act, and make the adjudication or dismiss the petition.

(e) If on the last day within which pleadings may be filed none are filed by the bankrupt or any of his creditors, the judge shall on the next day, if present, or as soon thereafter as practicable, make the adjudication or dismiss the petition.

(f) If the judge is absent from the district, or the division of the district in which the petition is pending, on the next day after the last day on which pleadings may be filed, and none have been filed by the bankrupt or any of his creditors, the clerk shall forthwith refer the case to the referee.

(g) Upon the filing of a voluntary petition the judge shall hear the petition and make the adjudication or dismiss the petition. If the judge is absent from the district, or the division of the district in which the petition is filed at the time of the filing, the clerk shall forthwith refer the case to the referee.

SECTION 19. *Jury trials.*—(a) A person against whom an involuntary petition has been filed shall be entitled to have a trial by jury, in respect to the question of his insolvency, except as herein otherwise provided, and any act of bankruptcy alleged in such petition to have been committed, upon filing a written application therefor at or before the time within which an answer may be filed. If such application is not filed within such time, a trial by jury shall be deemed to have been waived.

(b) If a jury is not in attendance upon the court, one may be specially summoned for the trial, or the case may be post-

poned, or, if the case is pending in one of the district courts within the jurisdiction of a circuit court of the United States, it may be certified for trial to the circuit court sitting at the same place, or by consent of parties when sitting at any other place in the same district, if such circuit court has or is to have a jury first in attendance.

(c) The right to submit matters in controversy, or an alleged offense under this act, to a jury shall be determined and enjoyed, except' as provided by this act, according to the United States laws now in force or such as may be hereafter enacted in relation to trials by jury.

SECTION 20. *Oaths, affirmations.*—(a) Oaths required by this act, except upon hearings in court, may be administered by (1) referees; (2) officers authorized to administer oaths in proceedings before the courts of the United States, or under the laws of the State where the same are to be taken; and (3) diplomatic or consular officers of the United States in any foreign country.

(b) Any person conscientiously opposed to taking an oath may, in lieu thereof, affirm. Any person who shall affirm falsely shall be punished as for the making of a false oath.

SECTION 21. *Evidence.*—(a) A court of bankruptcy may, upon application of any officer, bankrupt, or creditor, by order require any designated person, including the bankrupt and his wife, to appear in court or before a referee or the judge of any State court, to be examined concerning the acts, conduct, or property of a bankrupt whose estate is in process of administration under this act: Provided, That the wife may be examined only touching business transacted by her or to which she is a party, and to determine the fact whether she has transacted or been a party to any business of the bankrupt.

(b) The right to take depositions in proceedings under this act shall be determined and enjoyed according to the United States laws now in force, or such as may be hereafter enacted relating to the taking of depositions, except as herein provided.

(c) Notice of the taking of depositions shall be filed with the referee in every case. When depositions are to be taken in

opposition to the allowance of a claim notice shall also be served upon the claimant, and when in opposition to a discharge notice shall also be served upon the bankrupt.

(d) Certified copies of proceedings before a referee, or of papers, when issued by the clerk or referee, shall be admitted as evidence with like force and effect as certified copies of the records of district courts of the United States are now or may hereafter be admitted as evidence.

(e) A certified copy of the order approving the bond of a trustee shall constitute conclusive evidence of the vesting in him of the title to the property of the bankrupt, and if recorded shall impart the same notice that a deed from the bankrupt to the trustee if recorded would have imparted had not bankruptcy proceedings intervened.

(f) A certified copy of an order confirming or setting aside a composition, or granting or setting aside a discharge, not revoked, shall be evidence of the jurisdiction of the court, the regularity of the proceedings, and of the fact that the order was made.

(g) A certified copy of an order confirming a composition shall constitute evidence of the revesting of the title of his property in the bankrupt, and if recorded shall impart the same notice that a deed from the trustee to the bankrupt if recorded would impart.

SECTION 22. *Reference of cases after adjudication.*—(a) After a person has been adjudged a bankrupt the judge may cause the trustee to proceed with the administration of the estate, or refer it (1) generally to the referee or specially with only limited authority to act in the premises or to consider and report upon specified issues; or (2) to any referee within the territorial jurisdiction of the court, if the convenience of parties in interest will be served thereby, or for cause, or if the bankrupt does not do business, reside, or have his domicile in the district.

(b) The judge may, at any time, for the convenience of parties or for cause, transfer a case from one referee to another.

SECTION 23. *Jurisdiction of United States and State courts.*—(a) The United States circuit courts shall have juris-

diction of all controversies at law and in equity, as distinguished from proceedings in bankruptcy, between trustees as such and adverse claimants concerning the property acquired or claimed by the trustees, in the same manner and to the same extent only as though bankruptcy proceedings had not been instituted and such controversies had been between the bankrupts and such adverse claimants.

(b) Suits by the trustee shall only be brought or prosecuted in the courts where the bankrupt, whose estate is being administered by such' trustee, might have brought or prosecuted them if proceedings in bankruptcy had not been instituted, unless by consent of the proposed defendant, except suits for the recovery of property under section sixty, subdivision b, and section sixty-seven, subdivision e.

(c) The United States circuit courts shall have concurrent jurisdiction with the courts of bankruptcy, within their respective territorial limits, of the offenses enumerated in this act.

SECTION 24. *Jurisdiction of appellate courts.*—(a) The Supreme Court of the United States, the circuit courts of appeals of the United States, and the supreme courts of the Territories, in vacation in chambers and during their respective terms, as now or as they may be hereafter held, are hereby invested with appellate jurisdiction of controversies arising in bankruptcy proceedings from the courts of bankruptcy from which they have appellate jurisdiction in other cases. The Supreme Court of the United States shall exercise a like jurisdiction from courts of bankruptcy not within any organized circuit of the United States and from the supreme court of the District of Columbia.

(b) The several circuit courts of appeal shall have jurisdiction in equity, either interlocutory or final, to superintend and revise in matter of law the proceedings of the several inferior courts of bankruptcy within their jurisdiction. Such power shall be exercised on due notice and petition by any party aggrieved.

SECTION 25. *Appeals and writs of error.*—(a) That appeals, as in equity cases, may be taken in bankruptcy proceedings from the courts of bankruptcy to the circuit court of

appeals of the United States, and to the supreme court of the Territories, in the following cases, to wit, (1) from a judgment adjudging or refusing to adjudge the defendant a bankrupt; (2) from a judgment granting or denying a discharge; and (3) from a judgment allowing or rejecting a debt or claim of five hundred dollars or over. Such appeal shall be taken within ten days after the judgment appealed from has been rendered, and may be heard and determined by the appellate court in term or vacation, as the case may be.

(b) From any final decision of a court of appeals, allowing or rejecting a claim under this act, an appeal may be had under such rules and within such time as may be prescribed by the Supreme Court of the United States, in the following cases and no other:

1. Where the amount in controversy exceeds the sum of two thousand dollars, and the question involved is one which might have been taken on appeal or writ of error from the highest court of a State to the Supreme Court of the United States; or

2. Where some Justice of the Supreme Court of the United States shall certify that in his opinion the determination of the question or questions involved in the allowance or rejection of such claim is essential to a uniform construction of this act throughout the United States.

(c) Trustees shall not be required to give bond when they take appeals or sue out writs of error.

(d) Controversies may be certified to the Supreme Court of the United States from other courts of the United States, and the former court may exercise jurisdiction thereof and issue writs of certiorari pursuant to the provisions of the United States laws now in force or such as may be hereafter enacted.

SECTION 26. *Arbitration of controversies.*—(a) The trustee may, pursuant to the direction of the court, submit to arbitration any controversy arising in the settlement of the estate.

(b) Three arbitrators shall be chosen by mutual consent, or one by the trustee, one by the other party to the controversy, and the third by the two so chosen, or if they fail to agree in

five days after their appointment the court shall appoint the third arbitrator.

(c) The written finding of the arbitrators, or a majority of them, as to the issues presented, may be filed in court and shall have like force and effect as the verdict of a jury.

SECTION 27. *Compromises.*—(a) The trustee may, with the approval of the court, compromise any controversy arising in the administration of the estate upon such terms as he may deem for the best interests of the estate.

SECTION 28. *Designation of newspapers.*—(a) Courts of bankruptcy shall by order designate a newspaper published within their respective territorial districts, and in the county in which the bankrupt resides or the major part of his property is situated, in which notices required to be published by this act and orders which the court may direct to be published shall be inserted. Any court may in a particular case, for the convenience of parties in interest, designate some additional newspaper in which notices and orders in such case shall be published.

SECTION 29. *Offenses.*—(a) A person shall be punished by imprisonment for a period not to exceed five years, upon conviction of the offense of having knowingly and fraudulently appropriated to his own use, embezzled, spent, or unlawfully transferred any property or secreted or destroyed any document belonging to a bankrupt estate which came into his charge as trustee.

(b) A person shall be punished, by imprisonment for a period not to exceed two years, upon conviction of the offense of having knowingly and fraudulently (1) concealed while a bankrupt, or after his discharge, from his trustee any of the property belonging to his estate in bankruptcy; or (2) made a false oath or account in, or in relation to, any proceeding in bankruptcy; or (3) presented under oath any false claim for proof against the estate of a bankrupt, or used any such claim in composition personally or by agent, proxy, or attorney, or as agent, proxy, or attorney; or (4) received any material amount of property from a bankrupt after the filing of the petition, with intent to defeat this act; or (5) extorted or

attempted to extort any money or property from any person as a consideration for acting or forbearing to act in bankruptcy proceedings.

(c) A person shall be punished by fine, not to exceed five hundred dollars, and forfeit his office, and the same shall thereupon become vacant, upon conviction of the offense of having knowingly (1) acted as a referee in a case in which he is directly or indirectly interested; or (2) purchased, while a referee, directly or indirectly, any property of the estate in bankruptcy of which he is referee; or (3) refused, while a referee or trustee, to permit a reasonable opportunity for the inspection of the accounts relating to the affairs of, and the papers and records of, estates in his charge by parties in interest when directed by the court so to do.

(d) A person shall not be prosecuted for any offense arising under this act unless the indictment is found or the information is filed in court within one year after the commission of the offense.

SECTION 30. *Rules, forms, and orders.*—(a) All necessary rules, forms, and orders as to procedure and for carrying this act into force and effect shall be prescribed, and may be amended from time to time, by the Supreme Court of the United States.

SECTION 31. *Computation of time.*—(a) Whenever time is enumerated by days in this act, or in any proceeding in bankruptcy, the number of days shall be computed by excluding the first and including the last, unless the last fall on a Sunday or holiday, in which event the day last included shall be the next day thereafter which is not a Sunday or a legal holiday.

SECTION 32. *Transfer of cases.*—(a) In the event petitions are filed against the same person, or against different members of a partnership, in different courts of bankruptcy each of which has jurisdiction, the cases shall be transferred, by order of the courts relinquishing jurisdiction, to and be consolidated by the one of such courts which can proceed with the same for the greatest convenience of parties in interest.

DIVISION FIFTH.

Officers, Their Duties and Compensation.

SECTION 33. *Creation of two officers.*—(a) The offices of referee and trustee are hereby created.

SECTION 34. *Appointment, removal, and districts of referees.*—(a) Courts of bankruptcy shall, within the territorial limits of which they respectively have jurisdiction, (1) appoint referees, each for a term of two years, and may, in their discretion, remove them because their services are not needed or for other cause; and (2) designate, and from time to time change, the limits of the districts of referees, so that each county, where the services of a referee are needed, may constitute at least one district.

SECTION 35. *Qualifications of referees.*—(a) Individuals shall not be eligible to appointment as referees unless they are respectively (1) competent to perform the duties of that office; (2) not holding any office of profit or emolument under the laws of the United States or of any State other than commissioners of deeds, justices of the peace, masters in chancery, or notaries public; (3) not related by consanguinity or affinity, within the third degree as determined by the common law, to any of the judges of the courts of bankruptcy or circuit courts of the United States, or of the justices or judges of the appellate courts of the districts wherein they may be appointed; and (4) residents of, or have their offices in, the territorial districts for which they are to be appointed.

SECTION 36. *Oaths of office of referees.*—(a) Referees shall take the same oath of office as that prescribed for judges of United States courts.

SECTION 37. *Number of referees.*—(a) Such number of referees shall be appointed as may be necessary to assist in expeditiously transacting the bankruptcy business pending in the various courts of bankruptcy.

SECTION 38. *Jurisdiction of referees.*—(a) Referees respectively are hereby invested, subject always to a review by the judge, within the limits of their districts as established

from time to time, with jurisdiction to (1) consider all petitions referred to them by the clerks and make the adjudications or dismiss the petitions; (2) exercise the powers vested in courts of bankruptcy for the administering of oaths to and the examination of persons as witnesses and for requiring the production of documents in proceedings before them, except the power of commitment; (3) exercise the powers of the judge for the taking possession and releasing of the property of the bankrupt in the event of the issuance by the clerk of a certificate showing the absence of a judge from the judicial district, or the division of the district, or his sickness, or inability to act; (4) perform such part of the duties, except as to questions arising out of the applications of bankrupts for compositions or discharges, as are by this act conferred on courts of bankruptcy and as shall be prescribed by rules or orders of the courts of bankruptcy of their respective districts, except as herein otherwise provided; and (5) upon the application of the trustee during the examination of the bankrupts, or other proceedings, authorize the employment of stenographers at the expense of the estates at a compensation not to exceed ten cents per folio for reporting and transcribing the proceedings.

SECTION 39. *Duties of referees.*—(a) Referees shall (1) declare dividends and prepare and deliver to trustees dividend sheets showing the dividends declared and to whom payable; (2) examine all schedules of property and lists of creditors filed by bankrupts and cause such as are incomplete or defective to be amended; (3) furnish such information concerning the estates in process of administration before them as may be requested by the parties in interest; (4) give notices to creditors as herein provided; (5) make up records embodying the evidence, or the substance thereof, as agreed upon by the parties in all contested matters arising before them, whenever requested to do so by either of the parties thereto, together with their findings therein, and transmit them to the judges; (6) prepare and file the schedules of property and lists of creditors required to be filed by the bankrupts, or cause the same to be done, when the bankrupts fail, refuse, or neglect

to do so; (7) safely keep, perfect, and transmit to the clerks the records, herein required to be kept by them, when the cases are concluded; (8) transmit to the clerks such papers as may be on file before them whenever the same are needed in any proceedings in courts, and in like manner secure the return of such papers after they have been used, or, if it be impracticable to transmit the original papers, transmit certified copies thereof by mail; (9) upon application of any party in interest, preserve the evidence taken or the substance thereof as agreed upon by the parties before them when a stenographer is not in attendance; and (10) whenever their respective offices are in the same cities or towns where the courts of bankruptcy convene, call upon and receive from the clerks all papers filed in courts of bankruptcy which have been referred to them.

(b) Referees shall not (1) act in cases in which they are directly or indirectly interested; (2) practice as attorneys and counselors at law in any bankruptcy proceedings; or (3) purchase, directly or indirectly, any property of an estate in bankruptcy.

SECTION 40. *Compensation of referees.*—(a) Referees shall receive as full compensation for their services, payable after they are rendered, a fee of fifteen dollars deposited with the clerk at the time the petition is filed in each case, except when a fee is not required from a voluntary bankrupt, and twenty-five cents for every proof of claim filed for allowance, to be paid from the estate, if any, as a part of the cost of administration, and from estates which have been administered before them one per centum commissions on all moneys disbursed to creditors by the trustee, or one-half of one per centum on the amount to be paid to creditors upon the confirmation of a composition.

(b) Whenever a case is transferred from one referee to another the judge shall determine the proportion in which the fee and commissions therefor shall be divided between the referees.

(c) In the event of the reference of a case being revoked before it is concluded, and when the case is specially referred, the judge shall determine what part of the fee and commissions shall be paid to the referee.

SECTION 41. *Contempts before referees.*—(a) A person shall not, in proceedings before a referee, (1) disobey or resist any lawful order, process or writ: (2) misbehave during a hearing or so near the place thereof as to obstruct the same; (3) neglect to produce, after having been ordered to do so, any pertinent document; or (4) refuse to appear after having been subpoenaed, or, upon appearing, refuse to take the oath as a witness, or, after having taken the oath, refuse to be examined according to law: Provided, That no person shall be required to attend as a witness before a referee at a place outside of the State of his residence, and more than one hundred miles from such place of residence, and only in case his lawful mileage and fee for one day's attendance shall be first paid or tendered to him.

(b) The referee shall certify the facts to the judge, if any person shall do any of the things forbidden in this section. The judge shall thereupon, in a summary manner, hear the evidence as to the acts complained of, and, if it is such as to warrant him in so doing, punish such person in the same manner and to the same extent as for a contempt committed before the court of bankruptcy, or commit such person upon the same conditions as if the doing of the forbidden act had occurred with reference to the process of, or in the presence of, the court.

SECTION 42. *Records of referees.*—(a) The records of all proceedings in each case before a referee shall be kept as nearly as may be in the same manner as records are now kept in equity cases in circuit courts of the United States.

(b) A record of the proceedings in each case shall be kept in a separate book or books, and shall, together with the papers on file, constitute the records of the case.

(c) The book or books containing a record of the proceedings shall, when the case is concluded before the referee, be certified to by him, and, together with such papers as are on file before him, be transmitted to the court of bankruptcy and shall there remain as a part of the records of the court.

SECTION 43. *Referee's absence or disability.*—(a) Whenever the office of a referee is vacant, or its occupant is absent

or disqualified to act, the judge may act, or may appoint another referee, or another referee holding an appointment under the same court may, by order of the judge, temporarily fill the vacancy.

SECTION 44. *Appointment of trustees.*—(a) The creditors of a bankrupt estate shall, at their first meeting after the adjudication or after a vacancy has occurred in the office of trustee, or after an estate has been reopened, or after a composition has been set aside or a discharge revoked, or if there is a vacancy in the office of trustee, appoint one trustee or three trustees of such estate. If the creditors do not appoint a trustee or trustees as herein provided, the court shall do so.

SECTION 45. *Qualifications of trustees.*—(a) Trustees may be (1) individuals who are respectively competent to perform the duties of that office, and reside or have an office in the judicial district within which they are appointed, or (2) corporations authorized by their charters or by law to act in such capacity and having an office in the judicial district within which they are appointed.

SECTION 46. *Death or removal of trustees.*—(a) The death or removal of a trustee shall not abate any suit or proceeding which he is prosecuting or defending at the time of his death or removal, but the same may be proceeded with or defended by his joint trustee or successor in the same manner as though the same had been commenced or was being defended by such joint trustee alone or by such successor.

SECTION 47. *Duties of trustees.*—(a) Trustees shall respectively (1) account for and pay over to the estates under their control all interest received by them upon property of such estate; (2) collect and reduce to money the property of the estates for which they are trustees, under the direction of the court, and close up the estate as expeditiously as is compatible with the best interests of the parties in interest; (3) deposit all money received by them in one of the designated depositories; (4) disburse money only by check or draft on the depositories in which it has been deposited; (5) furnish such information concerning the estates of which they are trustees and their administration as may be requested by

parties in interest; (6) keep regular accounts showing all amounts received and from what sources and all amounts expended and on what accounts; (7) lay before the final meeting of the creditors detailed statements of the administration of the estates; (8) make final reports and file final accounts with the courts fifteen days before the days fixed for the final meetings of the creditors; (9) pay dividends within ten days after they are declared by the referees; (10) report to the courts, in writing, the condition of the estates and the amounts of money on hand, and such other details as may be required by the courts, within the first month after their appointment and every two months thereafter, unless otherwise ordered by the courts; and (11) set apart the bankrupt's exemptions and report the items and estimated value thereof to the court as soon as practicable after their appointment.

(b) Whenever three trustees have been appointed for an estate, the concurrence of at least two of them shall be necessary to the validity of their every act concerning the administration of the estate.

(c) The trustee shall, within thirty days after the adjudication, file a certified copy of the decree of adjudication in the office where conveyances of real estate are recorded in every county where the bankrupt owns real estate not exempt from execution, and pay the fee for such filing, and he shall receive a compensation of fifty cents for each copy so filed, which, together with the filing fee, shall be paid out of the estate of the bankrupt as a part of the cost and disbursements of the proceedings.

SECTION 48. *Compensation of trustees.*—(a) Trustees shall receive for their services, payable after they are rendered, a fee of five dollars deposited with the clerk at the time the petition is filed in each case, except when a fee is not required from a voluntary bankrupt, and from estates which they have administered such commissions on all moneys disbursed by them as may be allowed by the courts, not to exceed six per centum on the first five hundred dollars or less, four per centum on moneys in excess of five hundred dollars and less than fifteen hundred dollars, two per centum on moneys in excess

of fifteen hundred dollars and less than ten thousand dollars, and one per centum on moneys in excess of ten thousand dollars. And in case of the confirmation of a composition after the trustee has qualified the court may allow him, as compensation, not to exceed one-half of one per centum of the amount to be paid the creditors on such composition.

(b) In the event of an estate being administered by three trustees instead of one trustee or by successive trustees, the court shall apportion the fees and commissions between them according to the services actually rendered, so that there shall not be paid to trustees for the administering of any estate a greater amount than one trustee would be entitled to.

(c) The court may, in its discretion, withhold all compensation from any trustee who has been removed for cause.

SECTION 49. *Accounts and papers of trustees.*—(a) The accounts and papers of trustees shall be open to the inspection of officers and all parties in interest.

SECTION 50. *Bonds of referees and trustees.*—(a) Referees, before assuming the duties of their offices, and within such time as the district courts of the United States having jurisdiction shall prescribe, shall respectively qualify by entering into bond to the United States in such sum as shall be fixed by such courts, not to exceed five thousand dollars, with such sureties as shall be approved by such courts, conditioned for the faithful performance of their official duties.

(b) Trustees before entering upon the performance of their official duties, and within ten days after their appointment, or within such further time, not to exceed five days, as the court may permit, shall respectively qualify by entering into bond to the United States, with such sureties as shall be approved by the courts, conditioned for the faithful performance of their official duties.

(c) The creditors of a bankrupt estate, at their first meeting after the adjudication, or after a vacancy has occurred in the office of trustee, or after an estate has been reopened, or after a composition has been set aside or a discharge revoked, if there is a vacancy in the office of trustee, shall fix the amount of the bond of the trustee; they may at any time increase the

amount of the bond. If the creditors do not fix the amount of the bond of the trustee as herein provided the court shall do so.

(*d*) The court shall require evidence as to the actual value of the property of sureties.

(*e*) There shall be at least two sureties upon each bond.

(*f*) The actual value of the property of the sureties, over and above their liabilities and exemptions, on each bond shall equal at least the amount of such bond.

(*g*) Corporations organized for the purpose of becoming sureties upon bonds, or authorized by law to do so, may be accepted as sureties upon the bonds of referees and trustees whenever the courts are satisfied that the rights of all parties in interest will be thereby amply protected.

(*h*) Bonds of referees, trustees, and designated depositories shall be filed of record in the office of the clerk of the court and may be sued upon in the name of the United States for the use of any person injured by a breach of their conditions.

(*i*) Trustees shall not be liable, personally or on their bonds, to the United States, for any penalties or forfeitures incurred by the bankrupts under this act, of whose estates they are respectively trustees.

(*j*) Joint trustees may give joint or several bonds.

(*k*) If any referee or trustee shall fail to give bond, as herein provided and within the time limited, he shall be deemed to have declined his appointment, and such failure shall create a vacancy in his office.

(*l*) Suits upon referees' bonds shall not be brought subsequent to two years after the alleged breach of the bond.

(*m*) Suits upon trustees' bonds shall not be brought subsequent to two years after the estate has been closed.

SECTION 51. *Duties of clerks.*—(*a*) Clerks shall respectively (1) account for, as for other fees received by them, the clerk's fee paid in each case and such other fees as may be received for certified copies of records which may be prepared for persons other than officers; (2) collect the fees of the clerk, referee, and trustee in each case instituted before filing

the petition, except the petition of a proposed voluntary bankrupt which is accompanied by an affidavit stating that the petitioner is without, and cannot obtain, the money with which to pay such fees; (3) deliver to the referees upon application all papers which may be referred to them, or, if the offices of such referees are not in the same cities or towns as the offices of such clerks, transmit such papers by mail, and in like manner return papers which were received from such referees after they have been used; (4) and within ten days after each case has been closed pay to the referee, if the case was referred, the fee collected for him, and to the trustee the fee collected for him at the time of filing the petition.

SECTION 52. *Compensation of clerks and marshals.*—(a) Clerks shall respectively receive as full compensation for their services to each estate, a filing fee of ten dollars, except when a fee is not required from a voluntary bankrupt.

(b) Marshals shall respectively receive from the estate where an adjudication in bankruptcy is made, except as herein otherwise provided, for the performance of their service in proceedings in bankruptcy, the same fees, and account for them in the same way, as they are entitled to receive for the performance of the same or similar services in other cases in accordance with laws now in force, or such as may be hereafter enacted, fixing the compensation of marshals.

SECTION 53. *Duties of attorney-general.*—(a) The Attorney-General shall annually lay before Congress statistical tables showing for the whole country, and by States, the number of cases during the year of voluntary and involuntary bankruptcy; the amount of the property of the estates; the dividends paid and the expenses of administering such estates; and such other like information as he may deem important.

SECTION 54. *Statistics of bankruptcy proceedings.*—(a) Officers shall furnish in writing and transmit by mail such information as is within their knowledge, and as may be shown by the records and papers in their possession, to the Attorney-General, for statistical purposes, within ten days after being requested by him to do so.

DIVISION SIXTH.

Creditors.

SECTION 55. *Meetings of creditors.*—(a) The court shall cause the first meeting of the creditors of a bankrupt to be held, not less than ten nor more than thirty days after the adjudication, at the county seat of the county in which the bankrupt has had his principal place of business, resided, or had his domicile; or if that place would be manifestly inconvenient as a place of meeting for the parties in interest, or if the bankrupt is one who does not do business, reside, or have his domicile within the United States, the court shall fix a place for the meeting which is the most convenient for parties in interest. If such meeting should by any mischance not be held within such time, the court shall fix the date, as soon as may be thereafter, when it shall be held.

(b) At the first meeting of creditors the judge or referee shall preside, and, before proceeding with the other business, may allow or disallow the claims of creditors there presented, and may publicly examine the bankrupt or cause him to be examined at the instance of any creditor.

(c) The creditors shall at each meeting take such steps as may be pertinent and necessary for the promotion of the best interests of the estate and the enforcement of this act.

(d) A meeting of creditors, subsequent to the first one, may be held at any time and place when all of the creditors who have secured the allowance of their claims sign a written consent to hold a meeting at such time and place.

(e) The court shall call a meeting of creditors whenever one-fourth or more in number of those who have proven their claims shall file a written request to that effect; if such request is signed by a majority of such creditors, which number represents a majority in amount of such claims, and contains a request for such meeting to be held at a designated place, the court shall call such meeting at such place within thirty days after the date of the filing of the request.

(f) Whenever the affairs of the estate are ready to be closed a final meeting of creditors shall be ordered.

SECTION 56. *Voters at meetings of creditors.*—(a) Creditors shall pass upon matters submitted to them at their meetings by a majority vote in number and amount of claims of all creditors whose claims have been allowed and are present, except as herein otherwise provided.

(b) Creditors holding claims which are secured or have priority shall not, in respect to such claims, be entitled to vote at creditors' meetings, nor shall such claims be counted in computing either the number of creditors or the amount of their claims, unless the amounts of such claims exceed the values of such securities or priorities, and then only for such excess.

SECTION 57. *Proof and allowance of claims.*—(a) Proof of claims shall consist of a statement under oath, in writing, signed by a creditor setting forth the claim, the consideration therefor, and whether any, and, if so what, securities are held therefor, and whether any, and, if so what, payments have been made thereon, and that the sum claimed is justly owing from the bankrupt to the creditor.

(b) Whenever a claim is founded upon an instrument of writing, such instrument, unless lost or destroyed, shall be filed with the proof of claim. If such instrument is lost or destroyed, a statement of such fact and of the circumstances of such loss or destruction shall be filed under oath with the claim. After the claim is allowed or disallowed, such instrument may be withdrawn by permission of the court, upon leaving a copy thereof on file with the claim.

(c) Claims after being proved may, for the purpose of allowance, be filed by the claimants in the court where the proceedings are pending, or before the referee if the case has been referred.

(d) Claims which have been duly proved shall be allowed, upon receipt by or upon presentation to the court, unless objection to their allowance shall be made by parties in interest, or their consideration be continued for cause by the court upon its own motion.

(e) Claims of secured creditors and those who have priority may be allowed to enable such creditors to participate in

the proceedings at creditors' meetings held prior to the determination of the value of their securities or priorities, but shall be allowed for such sum only as to the courts seem to be owing over and above the value of their securities or priorities.

(f) Objections to claims shall be heard and determined as soon as the convenience of the court and the best interests of the estates and the claimants will permit.

(g) The claims of creditors who have received preferences, voidable under section sixty, subdivision b, or to whom conveyances, transfers, assignments, or incumbrances, void or voidable under section sixty-seven, subdivision e, have been made or given, shall not be allowed unless such creditors shall surrender such preferences, conveyances, transfers, assignments, or incumbrances.

(h) The value of securities held by secured creditors shall be determined by converting the same into money according to the terms of the agreement pursuant to which such securities were delivered to such creditors or by such creditors and the trustee, by agreement, arbitration, compromise, or litigation, as the court may direct, and the amount of such value shall be credited upon such claims, and a dividend shall be paid only on the unpaid balance.

(i) Whenever a creditor, whose claim against a bankrupt estate is secured by the individual undertaking of any person, fails to prove such claim, such person may do so in the creditor's name, and if he discharge such undertaking in whole or in part he shall be subrogated to that extent to the rights of the creditor.

(j) Debts owing to the United States, a State, a county, a district, or a municipality as a penalty or forfeiture shall not be allowed, except for the amount of the pecuniary loss sustained by the act, transaction, or proceeding out of which the penalty or forfeiture arose, with reasonable and actual costs occasioned thereby and such interest as may have accrued thereon according to law.

(k) Claims which have been allowed may be reconsidered for cause and reallocated or rejected in whole or in part, accord-

ing to the equities of the case, before but not after the estate has been closed.

(*l*) Whenever a claim shall have been reconsidered and rejected, in whole or in part, upon which a dividend has been paid, the trustee may recover from the creditor the amount of the dividend received upon the claim if rejected in whole or the proportional part thereof if rejected only in part.

(*m*) The claim of any estate which is being administered in bankruptcy against any like estate may be proved by the trustee and allowed by the court in the same manner and upon like terms as the claims of other creditors.

(*n*) Claims shall not be proved against a bankrupt estate subsequent to one year after the adjudication; or if they are liquidated by litigation and the final judgment therein is rendered within thirty days before or after the expiration of such time, then within sixty days after the rendition of such judgment: Provided, That the right of infants and insane persons without guardians, without notice of the proceedings, may continue six months longer.

SECTION 58. *Notice to creditors.*—(*a*) Creditors shall have at least ten days' notice by mail, to their respective addresses as they appear in the list of creditors of the bankrupt, or as afterwards filed with the papers in the case by the creditors, unless they waive notice in writing, of (1) all examinations of the bankrupt; (2) all hearings upon applications for the confirmation of compositions or the discharge of bankrupts; (3) all meetings of creditors; (4) all proposed sales of property; (5) the declaration and time of payment of dividends; (6) the filing of the final accounts of the trustee, and the time when and the place where they will be examined and passed upon; (7) the proposed compromise of any controversy, and (8) the proposed dismissal of the proceedings.

(*b*) Notice to creditors of the first meeting shall be published at least once and may be published such number of additional times as the court may direct; the last publication shall be at least one week prior to the date fixed for the meeting. Other notices may be published as the court shall direct.

(*c*) All notices shall be given by the referee, unless otherwise ordered by the judge.

SECTION 59. *Who may file and dismiss petitions.*—(a) Any qualified person may file a petition to be adjudged a voluntary bankrupt.

(b) Three or more creditors who have provable claims against any person which amount in the aggregate in excess of the value of securities held by them, if any, to five hundred dollars or over; or if all of the creditors of such person are less than twelve in number, then one of such creditors whose claim equals such amount may file a petition to have him adjudged a bankrupt.

(c) Petitions shall be filed in duplicate, one copy for the clerk and one for service on the bankrupt.

(d) If it be averred in the petition that the creditors of the bankrupt are less than twelve in number, and less than three creditors have joined as petitioners therein, and the answer avers the existence of a larger number of creditors, there shall be filed with the answer a list under oath of all the creditors, with their addresses, and thereupon the court shall cause all such creditors to be notified of the pendency of such petition and shall delay the hearing upon such petition for a reasonable time, to the end that parties in interest shall have an opportunity to be heard; if upon such hearing it shall appear that a sufficient number have joined in such petition, or if prior to or during such hearing a sufficient number shall join therein, the case may be proceeded with, but otherwise it shall be dismissed.

(e) In computing the number of creditors of a bankrupt for the purpose of determining how many creditors must join in the petition, such creditors as were employed by him at the time of the filing of the petition or are related to him by consanguinity or affinity within the third degree, as determined by the common law, and have not joined in the petition, shall not be counted.

(f) Creditors other than original petitioners may at any time enter their appearance and join in the petition, or file an answer and be heard in opposition to the prayer of the petition.

(g) A voluntary or involuntary petition shall not be dismissed by the petitioner or petitioners or for want of prosecution or by consent of parties until after notice to the creditors.

SECTION 60. *Preferred creditors.*—(a) A person shall be deemed to have given a preference if, being insolvent, he has, within four months before the filing of the petition, or after the filing of the petition and before the adjudication, procured or suffered a judgment to be entered against himself in favor of any person, or made a transfer of any of his property, and the effect of the enforcement of such judgment or transfer will be to enable any one of his creditors to obtain a greater percentage of his debt than any other of such creditors of the same class. Where the preference consists in a transfer, such period of four months shall not expire until four months after the date of the recording or registering of the transfer, if by law such recording or registering is required.

(b) If a bankrupt shall have given a preference, and the person receiving it, or to be benefited thereby, or his agent acting therein, shall have had reasonable cause to believe that it was intended thereby to give a preference, it shall be voidable by the trustee, and he may recover the property or its value from such person. And, for the purpose of such recovery, any court of bankruptcy, as hereinbefore defined, and any State court which would have had jurisdiction if bankruptcy had not intervened, shall have concurrent jurisdiction.

(c) If a creditor has been preferred, and afterwards in good faith gives the debtor further credit without security of any kind for property which becomes a part of the debtor's estates, the amount of such new credit remaining unpaid at the time of the adjudication in bankruptcy may be set off against the amount which would otherwise be recoverable from him.

(d) If a debtor shall, directly or indirectly, in contemplation of the filing of a petition by or against him, pay money or transfer property to an attorney and counselor at law, solicitor in equity, or proctor in admiralty for services to be rendered, the transaction shall be re-examined by the court on petition of the trustee or any creditor and shall only be held valid to the extent of a reasonable amount to be determined by the court, and the excess may be recovered by the trustee for the benefit of the estate.

DIVISION SEVENTH.

Estates.

SECTION 61. *Depositories for money.*—(a) Courts of bankruptcy shall designate, by order, banking institutions as depositories for the money of bankrupt estates, as convenient as may be to the residences of trustees, and shall require bonds to the United States, subject to their approval, to be given by such banking institutions, and may from time to time as occasion may require, by like order increase the number of depositories or the amount of any bond or change such depositories.

SECTION 62. *Expenses of administering estates.*—(a) The actual and necessary expenses incurred by officers in the administration of estates shall, except where other provisions are made for their payment, be reported in detail, under oath, and examined and approved or disapproved by the court. If approved, they shall be paid or allowed out of the estates in which they were incurred.

SECTION 63. *Debts which may be proved.*—(a) Debts of the bankrupt may be proved and allowed against his estate which are (1) a fixed liability, as evidenced by a judgment or an instrument in writing, absolutely owing at the time of the filing of the petition against him, whether then payable or not, with any interest thereon which would have been recoverable at that date or with a rebate of interest upon such as were not then payable and did not bear interest; (2) due as costs taxable against an involuntary bankrupt who was at the time of the filing of the petition against him plaintiff in a cause of action which would pass to the trustee and which the trustee declines to prosecute after notice; (3) founded upon a claim for taxable costs incurred in good faith by a creditor before the filing of the petition in an action to recover a provable debt; (4) founded upon an open account, or upon a contract express or implied; and (5) founded upon provable debts reduced to judgments after the filing of the petition and before the consideration of the bankrupt's application for a discharge, less costs incurred and interests accrued after the filing of the petition and up to the time of the entry of such judgments.

(b) Unliquidated claims against the bankrupt may, pursuant to application to the court, be liquidated in such manner as it shall direct, and may thereafter be proved and allowed against his estate.

SECTION 64. *Debts which have priority.*—(a) The court shall order the trustee to pay all taxes legally due and owing by the bankrupt to the United States, State, county, district, or municipality in advance of the payment of dividends to creditors, and upon filing the receipts of the proper public officers for such payment he shall be credited with the amount thereof, and in case any question arises as to the amount or legality of any such tax the same shall be heard and determined by the court.

(b) The debts to have priority, except as herein provided, and to be paid in full out of bankrupt estates, and the order of payment shall be (1) the actual and necessary cost of preserving the estate subsequent to filing the petition; (2) the filing fees paid by creditors in involuntary cases, and, where property of the bankrupt, transferred or concealed by him either before or after the filing of the petition, shall have been recovered for the benefit of the estate of the bankrupt by the efforts and at the expense of one or more creditors, the reasonable expenses of such recovery; (3) the cost of administration, including the fees and mileage payable to witnesses as now or hereafter provided by the laws of the United States, and one reasonable attorney's fee for the professional services actually rendered, irrespective of the number of attorneys employed, to the petitioning creditors in involuntary cases, to the bankrupt in involuntary cases while performing the duties herein prescribed, and to the bankrupt in voluntary cases, as the court may allow; (4) wages due to workmen, clerks, or servants which have been earned within three months before the date of the commencement of proceedings, not to exceed three hundred dollars to each claimant; and (5) debts owing to any person who by the laws of the States or the United States is entitled to priority.

(c) In the event of the confirmation of a composition being set aside, or a discharge revoked, the property acquired by the

bankrupt in addition to his estate at the time the composition was confirmed or the adjudication was made shall be applied to the payment in full of the claims of creditors for property sold to him on credit, in good faith, while such composition or discharge was in force, and the residue, if any, shall be applied to the payment of the debts which were owing at the time of the adjudication.

SECTION 65. *Declaration and payment of dividends.*—(a) Dividends of an equal per centum shall be declared and paid on all allowed claims, except such as have priority or are secured.

(b) The first dividend shall be declared within thirty days after the adjudication, if the money of the estate in excess of the amount necessary to pay the debts which have priority and such claims as have not been, but probably will be, allowed equals five per centum or more of such allowed claims. Dividends subsequent to the first shall be declared upon like terms as the first and as often as the amount shall equal ten per centum or more and upon closing the estate. Dividends may be declared oftener and in smaller proportions if the judge shall so order: Provided, That the first dividend shall not include more than fifty per centum of the money of the estate in excess of the amount necessary to pay the debts which have priority and such claims as probably will be allowed: And provided further, That the final dividend shall not be declared within three months after the first dividend shall be declared.

(c) The rights of creditors who have received dividends, or in whose favor final dividends have been declared, shall not be affected by the proof and allowance of claims subsequent to the date of such payment or declarations of dividends; but the creditors proving and securing the allowance of such claims shall be paid dividends equal in amount to those already received by the other creditors if the estate equals so much before such other creditors are paid any further dividends.

(d) Whenever a person shall have been adjudged a bankrupt by a court without the United States and also by a court of bankruptcy, creditors residing within the United States shall first be paid a dividend equal to that received in the court

without the United States by other creditors before creditors who have received a dividend in such court shall be paid any amounts.

(e) A claimant shall not be entitled to collect from a bankrupt estate any greater amount than shall accrue pursuant to the provisions of this act.

SECTION 66. *Unclaimed dividends.*—(a) Dividends which remain unclaimed for six months after the final dividend has been declared shall be paid by the trustee into court.

(b) Dividends remaining unclaimed for one year shall, under the direction of the court, be distributed to the creditors whose claims have been allowed but not paid in full, and after such claims have been paid in full the balance shall be paid to the bankrupt: Provided, That in case unclaimed dividends belong to minors such minors may have one year after arriving at majority to claim such dividends.

SECTION 67. *Liens.*—(a) Claims which for want of record or for other reasons would not have been valid liens as against the claims of the creditors of the bankrupt shall not be liens against his estate.

(b) Whenever a creditor is prevented from enforcing his rights as against a lien created, or attempted to be created, by his debtor, who afterwards becomes a bankrupt, the trustee of the estate of such bankrupt shall be subrogated to and may enforce such rights of such creditor for the benefit of the estate.

(c) A lien created by or obtained in or pursuant to any suit or proceeding at law or in equity, including an attachment upon mesne process or a judgment by confession, which was begun against a person within four months before the filing of a petition in bankruptcy by or against such person shall be dissolved by the adjudication of such person to be a bankrupt if (1) it appears that said lien was obtained and permitted while the defendant was insolvent and that its existence and enforcement will work a preference, or (2) the party or parties to be benefited thereby had reasonable cause to believe the defendant was insolvent and in contemplation of bankruptcy, or (3) that such lien was sought and permitted in fraud of the

provisions of this act; or if the dissolution of such lien would militate against the best interests of the estate of such person the same shall not be dissolved, but the trustee of the estate of such person, for the benefit of the estate, shall be subrogated to the rights of the holder of such lien and empowered to perfect and enforce the same in his name as trustee with like force and effect as such holder might have done had not bankruptcy proceedings intervened.

(*d*) Liens given or accepted in good faith and not in contemplation of or in fraud upon this act, and for a present consideration, which have been recorded according to law, if record thereof was necessary in order to impart notice, shall not be affected by this act.

(*e*) That all conveyances, transfers, assignments, or incumbrances of his property, or any part thereof, made or given by a person adjudged a bankrupt under the provisions of this act subsequent to the passage of this act and within four months prior to the filing of the petition, with the intent and purpose on his part to hinder, delay, or defraud his creditors, or any of them, shall be null and void as against the creditors of such debtor, except as to purchasers in good faith and for a present fair consideration; and all property of the debtor conveyed, transferred, assigned, or encumbered as aforesaid shall, if he be adjudged a bankrupt, and the same is not exempt from execution and liability for debts by the law of his domicile, be and remain a part of the assets and estate of the bankrupt and shall pass to his said trustee, whose duty it shall be to recover and reclaim the same by legal proceedings or otherwise for the benefit of the creditors. And all conveyances, transfers, or incumbrances of his property made by a debtor at any time within four months prior to the filing of the petition against him, and while insolvent, which are held null and void as against the creditors of such debtor by the laws of the State, Territory, or District in which such property is situate, shall be deemed null and void under this act against the creditors of such debtor if he be adjudged a bankrupt, and such property shall pass to the assignee and be by him reclaimed and recovered for the benefit of the creditors of the bankrupt. For the

purpose of such recovery any court of bankruptcy as herein-before defined, and any State court which would have had jurisdiction if bankruptcy had not intervened, shall have concurrent jurisdiction.

(f) That all levies, judgments, attachments, or other liens, obtained through legal proceedings against a person who is insolvent, at any time within four months prior to the filing of a petition in bankruptcy against him, shall be deemed null and void in case he is adjudged a bankrupt, and the property affected by the levy, judgment, attachment, or other lien shall be deemed wholly discharged and released from the same, and shall pass to the trustee as a part of the estate of the bankrupt, unless the court shall, on due notice, order that the right under such levy, judgment, attachment, or other lien shall be preserved for the benefit of the estate; and thereupon the same may pass to and shall be preserved by the trustee for the benefit of the estate as aforesaid. And the court may order such conveyance as shall be necessary to carry the purposes of this section into effect: Provided, That nothing herein contained shall have the effect to destroy or impair the title obtained by such levy, judgment, attachment, or other lien, of a bona fide purchaser for value who shall have acquired the same without notice or reasonable cause for inquiry.

SECTION 68. *Set-offs and counterclaims.*—(a) In all cases of mutual debts or mutual credits between the estate of a bankrupt and a creditor the account shall be stated and one debt shall be set off against the other, and the balance only shall be allowed or paid.

(b) A set-off or counterclaim shall not be allowed in favor of any debtor of the bankrupt which (1) is not provable against the estate; or (2) was purchased by or transferred to him after the filing of the petition, or within four months before such filing, with a view to such use and with knowledge or notice that such bankrupt was insolvent, or had committed an act of bankruptcy.

SECTION 69. *Possession of property.*—(a) A judge may, upon satisfactory proof, by affidavit, that a bankrupt against whom an involuntary petition has been filed and is pending

has committed an act of bankruptcy, or has neglected or is neglecting, or is about to so neglect his property that it has thereby deteriorated or is thereby deteriorating or is about thereby to deteriorate in value, issue a warrant to the marshal to seize and hold it subject to further orders. Before such warrant is issued the petitioners applying therefor shall enter into a bond in such an amount as the judge shall fix, with such sureties as he shall approve, conditioned to indemnify such bankrupt for such damages as he shall sustain in the event such seizure shall prove to have been wrongfully obtained. Such property shall be released, if such bankrupt shall give bond in a sum which shall be fixed by the judge, with such sureties as he shall approve, conditioned to turn over such property, or pay the value thereof in money to the trustee, in the event he is adjudged a bankrupt pursuant to such petition.

SECTION 70. *Title to property.*—(a) The trustee of the estate of a bankrupt, upon his appointment and qualification, and his successor or successors, if he shall have one or more, upon his or their appointment and qualification shall in turn be vested by operation of law with the title of the bankrupt, as of the date he was adjudged a bankrupt, except in so far as it is to property which is exempt, to all (1) documents relating to his property; (2) interests in patents, patent rights, copy-rights, and trade-marks; (3) powers which he might have exercised for his own benefit, but not those which he might have exercised for some other person; (4) property transferred by him in fraud of his creditors; (5) property which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him: Provided, That when any bankrupt shall have any insurance policy which has a cash surrender value payable to himself, his estate, or personal representatives, he may, within thirty days after the cash surrender value has been ascertained and stated to the trustee by the company issuing the same, pay or secure to the trustee the sum so ascertained and stated, and continue to hold, own, and carry such policy free from the claims of the creditors

participating in the distribution of his estate under the bankruptcy proceedings, otherwise the policy shall pass to the trustee as assets; and (6) rights of action arising upon contracts or from the unlawful taking or detention of, or injury to, his property.

(b) All real and personal property belonging to bankrupt estates shall be appraised by three disinterested appraisers; they shall be appointed by, and report to, the court. Real and personal property shall, when practicable, be sold subject to the approval of the court; it shall not be sold otherwise than subject to the approval of the court for less than seventy-five per centum of its appraised value.

(c) The title to property of a bankrupt estate which has been sold, as herein provided, shall be conveyed to the purchaser by the trustee.

(d) Whenever a composition shall be set aside, or discharge revoked, the trustee shall, upon his appointment and qualification, be vested as herein provided with the title to all of the property of the bankrupt as of the date of the final decree setting aside the composition or revoking the discharge.

(e) The trustee may avoid any transfer by the bankrupt of his property which any creditor of such bankrupt might have avoided, and may recover the property so transferred, or its value, from the person to whom it was transferred, unless he was a bona fide holder for value prior to the date of the adjudication. Such property may be recovered or its value collected from whoever may have received it, except a bona fide holder for value. For the purpose of such recovery any court of bankruptcy as hereinbefore defined, and any State court which would have had jurisdiction if bankruptcy had not intervened, shall have concurrent jurisdiction.

(f) Upon the confirmation of a composition offered by a bankrupt, the title to his property shall thereupon revert in him.

SECTION 71. That the clerks of the several district courts of the United States shall prepare and keep in their respective offices complete and convenient indexes of all petitions and discharges in bankruptcy heretofore or hereafter filed in the said courts, and shall, when requested so to do,

issue certificates of search certifying as to whether or not any such petitions or discharges have been filed; and said clerks shall be entitled to receive for such certificates the same fees as now allowed by law for certificates as to judgments in said courts; Provided, That said bankruptcy indexes and dockets, shall at all times be open to inspection and examination by all persons or corporations without any fee or charge therefor.

SECTION 72. That neither the referee nor the trustee shall in any form or guise receive, nor shall the court allow them, any other or further compensation for their services than that expressly authorized and prescribed in this act.

(B) FORMS OF ACCOUNTS IN BANKRUPTCY PROCEDURE.

The following are specimens of accounts, one made by a receiver in bankruptcy, and the other by the same person as trustee. Sometimes it is necessary to appoint a temporary caretaker, called a receiver, to preserve the estate before the time arrives when the creditors can legally appoint a trustee. The court chooses the receiver, and the creditors usually retain him in control when they come to select a trustee. When a receiver is continued in office as trustee, he usually waits for payment for all his services until distribution is made under his account as trustee. In some cases the receiver is not authorized to pay out any money, but is merely to act as custodian of the estate. The scope of his authority largely depends on the order of the court by which he is appointed, and care should be taken to draw up the order for the court to sign in such terms that the receiver will enjoy comprehensive powers.

IN THE DISTRICT COURT OF THE UNITED STATES FOR THE
EASTERN DISTRICT OF PENNSYLVANIA.

In the matter of	}	IN BANKRUPTCY.
JOHN DOE,		No. 637.
Bankrupt.		

First and Final Account of Edwin Maul, Receiver.

1906.

DR.

Jan. 2.—To inventory value of bankrupt's merchandise stock as per appraisalment filed...	\$4,500.00
" 3.—To cash received from Equitable Trust Co.	600.00
" 5.—To cash received from John Smith.....	45.00
	\$5,145.00

1906.

CR.

Jan. 5.—By cash paid C. Loebenthal, insurance of merchandise	\$5.00
Feb. 15.—By cash paid Thomas Dunn, watchman, for services to date	30.00
" 15.—By cash paid George Cole, Peter Linn and Owen Dunn, appraisers (\$20 each)	60.00
" 15.—By cash paid, affidavit to this account...	50
" 15.—By balance turned over to Edwin Maul, Trustee	5,049.50
	\$5,145.00

[Signed] EDWIN MAUL.

UNITED STATES OF AMERICA, }
EASTERN DISTRICT OF PENNSYLVANIA, } ss.:

Edwin Maul, being duly sworn according to law, deposes and says that the foregoing account is just and true, both as to items of charge and discharge.

[Signed] EDWIN MAUL.

Sworn to and subscribed before }
me, this 15th day of Feb- }
ruary, A. D. 1906. }
(Notarial seal, etc.)

The trustee's account is often accompanied with a brief report of his management of the estate. A specimen report is given below.

IN THE DISTRICT COURT OF THE UNITED STATES FOR THE
EASTERN DISTRICT OF PENNSYLVANIA.

In the matter of	}	IN BANKRUPTCY.
JOHN DOE,		
<i>Bankrupt.</i>		
		No. 637.

Report and Final Account of Edwin Maul, Trustee.

The trustee reports that he made diligent efforts to sell the stock of merchandise which constituted the principal asset of the estate. Several offers to buy the stock at private sale were received, but were rejected at a meeting of the creditors. It was then put up at public auction, and the best bid was made by Albert Kemp. Mr. Kemp offered to take the stock as a whole at \$4,800, which exceeded the appraised value by \$300. Some creditors objected to the confirmation of this sale, but after two meetings and further efforts to obtain a better bid, it was finally confirmed.

The trustee's account is as follows :

DR.

1906.

Feb. 16.—To cash and inventoried effects received from Edwin Maul, Receiver	\$5,049.50
May 31.—To cash received from Albert Kemp, merchandise stock, in excess of inventory valuation	300.00
June 1.—To cash received from William Waters, balance due by him to bankrupt on merchandise account	26.50
	\$5,376.00

CR.

1906.

May 31.—By cash paid S. T. Lorne & Co., commis-	
sions on sale of stock	\$240.00
“ 31.—By cash paid S. T. Lorne & Co., adver-	
tising sale and printing notices	25.00
June 1.—By cash paid Arthur Harris, watchman,	
for services from February 16 to date	100.00
“ 10.—By cash paid, affidavit to this account..	.50
Balance	5,010.50
	\$5,376.00

[Signed] EDWIN MAUL.

Bills Unpaid.

Costs, commissions and filing fees of William Noble, Esq., referee; fee of Joseph Warren, Esq., attorney for receiver and trustee; fee of Edgar Hughes, Esq., attorney for bankrupt; fee of Martin Gay, Esq., attorney for petitioning creditors; commissions of Edwin Maul, receiver and trustee.

UNITED STATES OF AMERICA, }
 EASTERN DISTRICT OF PENNSYLVANIA, } ss.:

Edwin Maul, being duly sworn according to law, deposes and says that the facts set forth in the foregoing account are just and true, both as to items of charge and discharge.

[Signed] EDWIN MAUL.

Sworn to and subscribed before }
 me, this 10th day of June, }
 A. D. 1906. }
 (Notarial seal, etc.)

The amount frequently paid to the auctioneers, as shown in the foregoing account, is five per cent of the sum realized upon the sale of the bankrupt's personal property. Often auctioneers claim a higher percentage, and it is wise to make

an agreement with them in the beginning. It will be noticed that the trustee's account mentions five unpaid bills. At the meeting of creditors called to pass upon the account, such unpaid bills are usually presented, and approved if found correct. It is wise for a trustee to consult with the referee and creditors before agreeing to pay lawyers' bills or other bills which may be disputed. The accounts stated above do not show the names of the creditors or the amounts of their claims. Ten days' notice of the consideration of the trustee's final account, and also of the meeting of creditors to declare dividends, is given to creditors. The declaration of a dividend may take place during the same meeting at which the trustee's account is considered. It is the duty of the referee, after ascertaining the final balance for distribution among creditors, to make up a dividend sheet. In accordance with the referee's calculations, the trustee makes out and signs checks for the various creditors, which the referee must countersign. The dividend checks are then distributed by the trustee ten days after the dividend is declared. It is a good practice for trustees to note either in a letter accompanying the check, or on the check itself: first, the amount of the creditor's claim, as allowed by the referee; and, second, the rate or percentage of the dividend declared. Payments of dividends, as well as all other payments made by a trustee or receiver, should be made by check. All moneys coming into his hands should be deposited at once to the credit of the estate in one of the depositories selected by the proper United States District Court for the use of bankrupt estates.

(C) THE PENNSYLVANIA INSOLVENCY ACT OF JUNE 4, 1901.

The insolvency act of 1901 has many features in common with the national bankrupt act, and both were passed for the same two main purposes. Both were meant to defeat attempts by insolvent debtors to prefer one creditor at another's expense. Both were meant also to secure a discharge for the debtor, under certain circumstances and upon compliance with certain

terms. The United States Constitution forbids a state to impair the obligation of a contract. Only the national government can do that. Consequently, the act of 1901, unlike the national bankrupt act, could not take away a creditor's rights without his consent. This consent the framers of the act planned to obtain, by inserting a provision that no creditor should share in the insolvent estate without first signing a release of the unpaid balance of his claim.

The act of 1901 provides a simpler, cheaper and quicker way of distributing an insolvent estate than the United States bankruptcy act, but the latter act prevents it from operating in many cases. The case of *Potts v. Manufacturing Co.* (1904), 25 Super. 206, shows that the Pennsylvania statute cannot usually be invoked to defeat a preference while the national statute remains in force. Potts obtained judgment against the manufacturing company, which made an assignment under the act of 1901 for the benefit of all its creditors. The assignee obtained an order from the Court of Common Pleas, setting aside the sheriff's proceedings by which Potts was endeavoring to sell the company's effects in order to satisfy his judgment. The court granted this order, in accordance with Section 16 of the Pennsylvania statute, because the assignment for creditors would be useless, if any individual creditor could sell the company's assets for his own private benefit.

Potts appealed to the Superior Court, on the ground that the existence of the United States bankrupt act provided a remedy in such cases, and that proceedings under the Pennsylvania act were, therefore, void. It did not appear that either the manufacturing company or any of its creditors had actually started proceedings under the national act, but the Superior Court decided that uniformity in administering insolvent estates can only be secured through the bankrupt act, and that the prosecution of proceedings under the laws of the various states tends to confusion. The order of the Common Pleas Court was, therefore, reversed, and Potts was allowed to go ahead with his sheriff's sale. The Supreme Court has never passed on this matter.

The chief reason for holding that the Pennsylvania act is largely inoperative, while the act of 1898 remains on the statute books, is that any proceeding under the state insolvency law might be superseded by the filing of a bankruptcy petition, where the debtor was subject to the operation of the national act. Section three of the bankrupt act authorizes creditors of an insolvent to start proceedings under it if the insolvent has "made a general assignment for the benefit of his creditors, or, being insolvent, applied for a receiver or trustee for his property, or because of insolvency a receiver or trustee has been put in charge of his property under the laws of a state, of a territory, or of the United States." Furthermore, the insolvent himself may upset an assignment under the Pennsylvania statute by filing a bankruptcy petition in the United States District Court, so as to get an absolute discharge under the national act.

The national act authorizes any person who owes a debt, except a corporation, to file a voluntary petition, and obtain the benefits conferred by it. Involuntary proceedings cannot, however, be started by the creditors of a wage-earner, so as to force him into bankruptcy against his will. The same exemption from involuntary proceedings is given to a person engaged chiefly in farming or the tillage of the soil, and also to national banks and banks incorporated under state or territorial laws: also to all other corporations except those engaged principally in manufacturing, trading, printing, publishing, mining or mercantile pursuits. A railway corporation, for instance, is not subject to the operation of the bankruptcy act.

The Pennsylvania act of 1901 is in force as to wage-earners, farmers and many of the corporations to which the national act does not fully apply. Not every insolvent corporation, however, which falls outside the range of the national act is subject to the Pennsylvania law. Insolvent national banks, for instance, are governed by the provisions of the national banking act. In the case of *Citizens' Bank v. Gass* (1905), 29 Super. 125, Gass claimed the benefit of the thirty-first section of the act of 1901. This gives an insolvent, whose

estate is being administered under the act, an absolute right to his exemption of \$300 and certain articles of personal property, although he may have waived his right to this exemption in some contract or judgment. Gass was a farmer, and in such a case the act of 1901 is fully operative. He obtained the exemption, therefore, although he had waived it in a judgment note given to the Citizens' Bank. The Pennsylvania statute is suspended only as to those who can be made subject against their will to the provisions of the national bankrupt act. See also the case of *Charles v. Smith* (1905), 29 Super. 594.

Some voluntary assignments under the act of 1901 are being made throughout Pennsylvania even by those who can be forced into involuntary bankruptcy under the national act. Proceedings under the State law are, as mentioned before, simpler, cheaper and quicker than bankruptcy proceedings, and, therefore, they are often preferred by all parties interested in an insolvent estate. The practical disadvantage is that a few dissatisfied creditors, whose claims amount to \$500, may ordinarily defeat the insolvency proceedings by filing an involuntary bankruptcy petition against the insolvent, except in the case of farmers, wage-earners and certain corporations. Such bankruptcy proceedings must be commenced within four months after the assignment for creditors is made under the Pennsylvania law.

The act of June 4, 1901, contains a form for proof of claims by creditors, and several other forms which must be followed in proceedings under it. The act is given below, except the last section repealing certain prior acts:

SECTION 1. *Certain preferences to benefit all creditors.*—If any person, persons, firm, limited partnership, joint-stock company or corporation, being insolvent or in contemplation of insolvency, with a view to give a preference to any creditor or person having a claim against, or who is under any liability for, such insolvent, shall procure, suffer or permit any judgment to be entered, by confession or otherwise, or any execution to be levied, or any attachment or sequestration to be made

of any part of his, their or its real or personal property, or shall make any payment, pledge, assignment, transfer, conveyance or incumbrance thereof, either absolutely or as collateral security for a debt then existing, whether due or not, such judgment, execution, attachment, sequestration, payment, pledge, assignment, transfer, conveyance, or incumbrance shall inure to the benefit of all the creditors of such insolvent, if an assignment for the benefit of creditors be made or proceedings in insolvency be commenced within four months after such judgment, execution, attachment, sequestration, payment, pledge, assignment, transfer, conveyance, or incumbrance shall have been entered, issued, commenced, made or recorded, and in the case of personal property exclusive possession given.

SECTION 2. *Collusion of creditor.*—If any person, persons, firm, limited partnership, joint-stock company or corporations, being insolvent or in contemplation of insolvency, with a view to give a preference to any creditor or person having a claim against, or who is under any liability for, such insolvent, shall procure, suffer or permit any judgment to be entered, by confession or otherwise, or any execution to be levied, or any attachment or sequestration to be made of any part of his, their or its real or personal property, or shall make any payment, pledge, assignment, transfer, conveyance, or incumbrance thereof, either absolutely or as collateral security for a debt then existing or about to be created, and if the aforesaid be known to such creditor, who thereby collusively attempts to obtain for himself or others a preference over other creditors, such judgment, execution, attachment, sequestration, payment, pledge, assignment, transfer, conveyance, or incumbrance shall inure to the benefit of all the creditors of such insolvent, if an assignment for the benefit of creditors be made or proceedings in insolvency be commenced within four months after such judgment, execution, attachment, sequestration, payment, pledge, assignment, transfer, conveyance, or incumbrance shall have been entered, issued, commenced, made or recorded, and in the case of personal property exclusive possession given. A presumption of such knowledge and intention shall arise, by reason of the fact of such insolvency, if the consideration be

grossly inadequate, or if such judgment, execution, attachment, sequestration, payment, pledge, assignment, transfer, conveyance, or incumbrance shall not have been entered, issued, commenced, made or recorded, and, in the case of personal property, exclusive possession be not given at or about the time of the creation of the debt, or if the transaction shall not have been made in the usual and ordinary course of the business of such insolvent. But nothing herein contained shall in any manner affect any judgment, payment, pledge, assignment, transfer, conveyance, or incumbrance taken in good faith, without such knowledge or intention, when a debt is created or about to be created, if entered, made or recorded, and in the case of personal property exclusive possession be given at or about that time.

SECTION 3. *Assignment.*—Any person, persons, firm, limited partnership, joint-stock company or corporation may make an assignment of his, their or its property to one or more disinterested persons, as assignees, not exceeding three, for the benefit of his, their or its creditors; but, except as herein otherwise provided, all preferences or conditions therein contained shall be wholly void, and such assignment shall unconditionally inure to the benefit of all the creditors accepting a dividend, as in this act provided. An assignment of a portion of such property in trust, for the benefit of the creditors, or any of them, however expressed, shall be deemed an assignment of the whole estate, and shall be recorded in the same counties, with the same effect, as a general assignment; but a debtor may assign any part of his estate to certain creditors, or in trust for them, if at the time of so doing he be solvent, or the same be not in contravention of the other provisions of this act.

SECTION 4. *Assignment of partnership assets.*—Any member or members of a partnership, limited or otherwise, except the associations created under the act of second June, one thousand eight hundred and seventy-four, and its supplements, or any one or more joint, or joint and several debtors, may make an assignment of the assets in which he or they are interested with others, for the benefit of their creditors, in the manner and with the effect herein provided; but any other person or per-

sons jointly, or jointly and severally, interested in such assets, may, within fifteen days after notice thereof, upon petition to the court and with notice to the assignors, give security to indemnify and save harmless the assignors, and to pay all debts, or to obtain the release of the assignors therefrom, within such time as the court shall designate, not exceeding six months; whereupon the assignees shall forthwith transfer to those entering such security all the assets passing by the assignment, freed and clear of all claims upon the part of the assignors and assignee, but the rights of the creditors shall remain as if no assignment had been made. In case of such an assignment, the assignee shall forthwith give written notice to the other person or persons jointly, or jointly and severally, interested in such assets, and shall file of record an affidavit thereof, and the fifteen days shall be computed from the time of such filing. If the assignment be set aside, the costs incurred, including the reasonable expenses and the fees of the assignees, shall be paid as the court shall direct.

SECTION 5. *Arrest on civil process.*—Any person arrested on civil process may make an assignment for the benefit of his creditors, in the manner herein set forth, and may thereupon present his petition to the court issuing the same, accompanied by the assignment, inventory, schedules and oath required, or copies thereof if the process was issued by a different court from that which has jurisdiction of such an assignment, and praying a rule to show cause why he should not be discharged from arrest. The court to which the petition is presented shall grant the rule, returnable at some convenient time, and, unless the case is one requiring the petitioner's imprisonment, shall discharge the petitioner pending the hearing of said rule, upon his paying the fees due the jailor, if any, and, upon his entering such security for his appearance, surrender and compliance with the decrees of the court and the requirements of this act, as the court shall deem requisite. Actual notice of the rule shall be given to the plaintiff in the process, or his counsel of record, and to all creditors whose addresses are known to petitioner; and publication thereof shall be made twice in a daily newspaper published in the county, and once in the legal

periodical, if any, designated by the court, and an affidavit of such service and publication shall be filed in the cause at least three days before the day fixed for the hearing. Notice to creditors non-resident in the county may be made by registered letter. Upon the hearing of the rule, which shall be at the bar of the court, and at which the petitioner shall answer all questions put to him and shall produce all papers and books required of him, if it shall appear to the court that the petitioner has duly assigned all his property for the benefit of his creditors, that he has not violated any of the provisions of this act, and that all the claims against him would be discharged by the creditors accepting a dividend, as by this act provided, the court shall forthwith discharge him from arrest; and he shall not thereafter be liable to arrest in said proceedings, or upon any claim existing at that time, unless upon petition to said court, and with notice to the insolvent, it shall afterwards be made to appear that, under this act, he should have been or should be imprisoned. If, however, he shall refuse to answer relevant questions, or to produce his books and papers, or it shall appear that he has violated any of the provisions of this act, or that any of the claims against him would not be discharged by the creditors accepting a dividend, as by this act provided, he shall be discharged from arrest only upon undergoing such imprisonment, not exceeding ninety days, as the court shall require. If the petitioner fails to give notice as required, or to appear, or to surrender himself within forty-eight hours, or to comply with the decrees of the court or the provisions of this act, his bond shall thereby be forfeited, and recovery may be had thereon by the assignee, for the use of all the creditors of the insolvent, and he may be rearrested by an alias or pluries writ. A surrender, to be valid, must be accompanied by a certified copy of the order of the court, or of the writ under which the arrest was originally made. The assignment once made shall proceed in the usual course. The benefits of this section shall not extend to any person who has been attached for failure to comply with an order or decree requiring him to make an assignment, execute a conveyance, or to do any other specific act, until he shall, in fact, have done

so, nor shall it in any manner affect the liability of the petitioner to imprisonment for crime.

SECTION 6. *Prisoners who may be discharged.*—The Court of Common Pleas of any county, in which any person may be confined by sentence or order of any court of this Commonwealth until he restore any stolen goods or chattels, or pay the value thereof; or in which any person may be confined for the non-payment of any fine or of the costs of prosecution, or upon conviction of fornication and bastardy, and for no other cause, shall discharge such person from confinement on his making application and conforming to the provisions herein directed in the case of insolvents, who have been arrested on civil process: Provided, That where such person shall have been sentenced to the payment of a fine, or after a conviction of fornication and bastardy, he shall not be entitled to make such application until after he shall have been in actual confinement for a period of not less than three months, except in case of a fine not exceeding fifteen dollars, exclusive of costs, in which event the actual confinement need not exceed thirty days.

SECTION 7. *Proceedings by a creditor of an alleged insolvent.*—Any creditor of an alleged insolvent may, in the Court of Common Pleas of the county where the alleged insolvent resides or his principal place of business is situate, by petition, under oath, aver that such person, persons, firm, limited partnership, joint-stock company or corporation is insolvent, has not made an assignment for the benefit of his, their or its creditors, is resident or is carrying on business in said county, and:—

(1) Has called a meeting of his creditors for the purpose of compounding with them, or has exhibited a statement showing his inability to meet his liabilities, or has otherwise acknowledged his insolvency; or,

(2) Has absconded or is about to abscond, with intent to defraud any creditor, or to defeat or delay the remedy of any creditor, or to avoid being arrested or served with legal process, or conceals himself within or remains out of the Commonwealth, with like intent; or,

(3) Secretes or is about to secrete any part of his estate or effects, with intent to defraud his creditors, or to defeat or delay their demands, or any of them; or,

(4) Has assigned, removed or disposed of, or is about to assign, remove or dispose of, any part of his property, with intent to defraud, defeat or delay his creditors, or any of them; or,

(5) Has been actually imprisoned for more than thirty days, in a civil action, or, being arrested therefor, has escaped from custody; or,

(6) Has refused or neglected to comply with any order, judgment or decree for the payment of money, and an execution therefor has been returned unsatisfied; or,

(7) Has suffered or permitted any attachment or sequestration to remain against any of his property, without attempting to dissolve, by rule taken for that purpose, or upon entering security for a period of thirty days, or having taken a rule to dissolve which has been discharged by the court, has not entered security within twenty days thereafter; or,

(8) Has made any pledge, assignment, transfer, conveyance or incumbrance of the whole or a large part of his stock in trade or property, without being able to meet his liabilities and without the consent of his creditors, either in payment of or as security for a debt then existing, or with the intent to prefer one creditor to another, or out of his usual course of business, or for the benefit of himself or family.

Whereupon, the court shall grant a rule to show cause why a receiver should not be appointed for the estate of such alleged insolvent, and all legal proceedings thereagainst, if any, vacated and set aside. Notice of said rule shall be given to the alleged insolvent and all other persons interested. If the facts averred are not denied, under oath, the court shall make such order as the facts averred or shown may require. If they are denied, testimony shall be taken at the bar of the court or by a law judge thereof, and the court shall make such order or decree as the facts found will justify, and may enforce the same by attachment of the person or sequestration of the property of the party in default. Any person, without founda-

tion, maliciously invoking the action of the court under this section, shall be liable for a sum equal to double the injury actually sustained by the alleged insolvent.

SECTION 8. *Receiver.*—In such proceedings, as soon as the fact of insolvency be made to appear, the court shall forthwith appoint a disinterested person as receiver, unless the insolvent has made an assignment for the benefit of his creditors or has given security to pay petitioner's debt. Property of a perishable nature or likely to deteriorate in value may be sold by leave of the court, the proceeds thereof to be substituted in lieu thereof.

SECTION 9. *Assignment to be filed.*—All such assignments shall be acknowledged before some person authorized to take the acknowledgment of deeds, and shall be forthwith recorded in the office of the recorder of deeds, where the debtor shall reside or his principal place of business is situate. Within five days thereafter a copy of said deed shall be filed by the assignor in the Court of Common Pleas of the said county together with: (one), A schedule of all the assets of said debtor, whether real or personal, and wheresoever situate, whether in possession, reversion, remainder or in trust, and whether presently valuable or otherwise, and stating what evidences there are or should be thereof, the present value as near as may be, and the liens or claims if any thereagainst; (two), a list of the creditors, with the amounts of their claims, the exact addresses of the creditors, how and where the debts arose, what evidences thereof there may be, and what security or claims against other persons the creditors may have for the payment of the same or any part thereof; (three), a full statement of the cause of his insolvency; (four), a list of all the judgments confessed, or payments, pledges, assignments, transfers, conveyances or incumbrances made by him in payment of, or as security for, a pre-existing debt, or for the benefit of himself or family, or with intent to prefer one creditor to another, or out of the usual and ordinary course of his business, within three months prior to his assignment, and the consideration therefor. And attached thereto shall be an oath by the insolvent in the following form:

I do swear (or affirm) that all the schedules above set forth are in all respects just and true; that I have not at any time, or in any manner whatsoever, since my insolvency, disposed of or made over any part of my estate for the future benefit of myself or my family, or in order to defraud any of my creditors; that I have, in no instance, credited or acknowledged a debt for a greater sum than I honestly and truly owed; that I have not preferred or attempted to prefer one creditor over another since my insolvency, except as in said schedule set forth; that I have not withheld, concealed, intrusted, or in any way disposed of or incumbered, any of my property which should justly be delivered over for the benefit of my creditors; that I have not changed, altered or falsified any of my books or papers, but have delivered the same to my assignees for the purposes of my estate; and that if any further assets of my estate come to my knowledge I will forthwith disclose or deliver the same to my assignee. So help me God (or, and so I do affirm).

SECTION 10. *Assignment or decree to be recorded.*—

The assignment or a certified copy of the decree of the court appointing a receiver shall be recorded in the county where the insolvent resides, or his principal place of business is situate, and in every county where he owns real estate. A failure to record shall not in any manner affect the assignment; but if the assignee fails to record it within fifteen days after its delivery, his compensation as assignee shall be reduced by a sum sufficient to pay the costs, expenses and counsel fees of any creditor, or creditors, who in ignorance thereof bring suit or proceed with one already brought, and such sums shall be paid to such creditors. Any creditor may compel the production and recording of an assignment, by petition to the proper Court of Common Pleas, at the expense and cost of the defaulting assignee, including a reasonable counsel fee to such creditor's attorney.

SECTION 11. *Form of oath of assignee or receiver.*—

The assignee or receiver shall, immediately after his appointment, take, subscribe to, and file in the proper court, an oath or affirmation in the following form:

I, A. B., do solemnly swear (or affirm) that I am legally qualified to act as assignee (or receiver) of the estate of C. D., an insolvent; that I am not interested therein or adversely thereto; that I will faithfully manage said estate for the benefit of the creditors thereof, in the manner provided by law, and will fully and accurately account for all the assets. So help me God (or, and so I do affirm).

SECTION 12. *Form of bond.*—The assignee or receiver shall, before entering on the performance of his duties, give bond, with sufficient sureties, to the Commonwealth, for the use and benefit of all parties in interest, in at least double the value of the insolvent's estate, as known to him, conditioned as follows:

The condition of this obligation is such that if the above bounden A. B., assignee (or receiver) of the estate of C. D., an insolvent, has discharged and shall faithfully discharge his duty as assignee, shall faithfully account for all moneys or assets received or to be received by him, or in which the estate of said insolvent is in any manner interested, and has faithfully executed and shall faithfully execute the trust confided to him, in the manner provided by law, then this obligation to be void; otherwise, to be and remain in full force and effect.

If additional assets are discovered after the giving of said bond, or the assets realize much more than their estimated value, or the court shall be of opinion that any of the bonds theretofore given is, for any cause, insufficient, the assignee or receiver shall give a new bond or bonds and with like conditions. Suits may be brought thereupon, as in the case of other official bonds, until the amounts thereof are exhausted; but neither said suits, nor the exhaustion of said bonds, shall in any way limit the liability of such assignee or receiver.

SECTION 13. *Delivery of assets.*—The insolvent shall forthwith deliver to the assignee or receiver all his assets; including all vouchers, notes, bonds, bills, securities or other evidences of debt, documents, muniments of title, and writings in any way relating to, or having any bearing upon, or connection with, his estate; all books of account, patents, copyrights, assignments, leases, agreements and, generally, every-

thing which relates to the assets, or will assist the assignee or receiver in collecting the same, or in ascertaining the true amount due to the creditors of the estate. The said insolvent shall, from time to time, at the expense of the estate, make and execute such deeds and writings, endorse such bills and other negotiable papers, draw such checks and orders for money deposited in banks and elsewhere, and do all such other lawful acts and things as the assignee or receiver may reasonably require, and which may be deemed useful for confirming the assignment, or to enable the assignee to demand, recover and receive all the estate and effects of the insolvent, especially any part thereof which is without this Commonwealth. The court may, by rule to show cause, followed by attachments for contempt, compel the insolvent to comply with its orders in this regard; but his failure or refusal so to do, either before or after such order, shall in nowise affect or impair the right of the assignee or receiver to recover any of the assets by suit, in his own name.

SECTION 14. *Assignee to give notice.*—Immediately after his appointment, the assignee shall give written or printed notice to all the creditors known to him of the fact of his appointment; notifying them that on a given day and hour, not more than twenty days distant, and at a given place, particularly designated, a meeting of all the creditors will be held, for the purpose of selecting an additional assignee or assignees, if they deem the same to be necessary. At such meeting a majority in amount of the creditors present, in person or by proxy,—partnerships or joint creditors however having but one vote each,—may select as many more assignees as there were assignees named in the original deed of assignment. The assignees originally named shall, by deed duly executed, acknowledged and recorded, transfer to those thus selected an equal and undivided interest in said estate, and all the assignees thus named and selected shall thereafter act as joint assignees, with the same effect as if all were originally named in the original deed of assignment.

SECTION 15. *Inventory to be filed. Examination of insolvent and others.*—The receiver within twenty days after

his appointment, and the assignees within twenty days after the meeting of the creditors, shall file a sworn inventory of the estate, with its then present value. For the purpose of enabling them to do so, or to file any supplementary inventory, they are hereby empowered to examine the insolvent, under oath, as to any matter appertaining to such assets, and by leave of the court to call before them, by subpoena, with or without his books and papers, or the books and papers of any firm, limited partnership, joint-stock company, or corporation with which he is connected; and examine also, under oath, on the same subject, any person who they have reason to believe has knowledge of other or further assets of the insolvent's estate, or can give them information touching the same. No objection to such examination shall be made on the ground that a disclosure would tend to bring the witness into contempt, or disgrace or convict him of crime; but the information thus obtained shall not be used against him in any other proceeding. Any witness may decline to answer any question, or produce any books and papers, which, aside from the foregoing, he would not be required to answer or to produce in court upon a trial involving the same questions. Every witness, including the insolvent, shall be entitled to receive, out of the insolvent's estate, the usual witness fee and mileage for his attendance for this purpose.

SECTION 16. *Vacation of attachments, etc.*—Upon application of the assignee or receiver, the court shall vacate and set aside all attachments, executions, sequestrations or other legal proceedings not wholly completed, and all money in court or in the hands of the sheriff, by virtue thereof, shall be paid to such assignee or receiver. The assignee or receiver shall pay, out of so much of the insolvent's estate as was attached, sequestered or levied upon, or was received from the court or sheriff, the legal cost of such vacated proceedings, as a preferred claim if the creditor's claim is afterwards allowed in the distribution of the insolvent's estate; and the creditor's claim shall also be paid thereout, if it shall be decided that, notwithstanding the provisions of this act, he was entitled to a preference.

SECTION 17. *Powers of assignee.*—An assignee or receiver for the benefit of creditors shall be under the control of the proper Court of Common Pleas; shall be the representative of the creditors of the insolvent, and entitled by proper legal steps, in his own name as assignee or receiver, to have vacated and set aside for the benefit of all the creditors any judgment, execution, attachment, sequestration, payment, pledge, assignment, transfer, conveyance or incumbrance which heretofore could have been avoided by the creditors, or any of them, or by which it is attempted to give one creditor preference over another, or which, by this act, inures to the benefit of all the creditors of such insolvent. He shall be vested with all the property of the insolvent, real or personal, which the insolvent could have sold, assigned or conveyed, or which might have been taken in execution, or otherwise made liable for his debts or engagements, or any of them, at law or in equity, including patents and copyrights, royalties, debts due to or for the insolvent, liens or securities therefor, and rights of action or redemption; and, by leave of and subject to the control of the court, may carry on any business in which the insolvent may have been engaged. Every beneficial power and the interest of any person entitled to compel the execution of a trust power, shall pass to the assignee or receiver of the person in whom such power or interest is vested. He may, by bill of discovery or other legal or equitable proceeding, obtain information of, and sue for and recover, in his own name as such assignee or receiver, any assets which the insolvent might sue for and recover, or which any of his creditors might make available in payment of their claims; and any recovery had shall inure to the benefit of all, in proportion to their respective demands. And he shall be liable to suit, in his representative capacity, by any person seeking to recover specific property, if such property could have been recovered as against the creditors of the insolvent levying an execution thereon: Provided,

I. That no purchase or assignment of the real or personal property of such insolvent, made *bona fide* and for a valuable consideration, before the recording of the assignment or of

the appointment of a receiver in the county where such purchase or assignment is made, by or to any person not having actual notice or knowledge of such insolvency, or of the assignment or petition, shall be invalidated or impeached thereby, unless voidable under the other provisions of this act:

II. That if any person indebted to such insolvent, or having possession of any of his property, shall *bona fide* pay the said debt or deliver the said property to the said insolvent, without having had actual notice or knowledge of such petition or assignment, he shall not be liable to pay or deliver the same to such assignee or receiver.

SECTION 18. *Public or private sale.*—The assignee or receiver within one year after his appointment, unless the court upon cause shown shall extend the time, shall collect all the moneys due to the insolvent; shall sell at public or private sale all the stocks, bonds, mortgages, evidences of debt and other like property of the insolvent, and shall sell at public sale the real and other personal property of the insolvent, unless upon cause shown the court shall authorize a private sale. After the expiration of that time the court may, upon cause shown, authorize a public or private sale of all the assets, of whatever kind or character the same may be, and wherever situate. All sales shall be for cash unless the court shall otherwise authorize. The purchaser from the assignee or receiver may maintain any action, regarding the property purchased, in his own name, or continue any action already brought to his use, with the same rights and to the same effect as the assignee or receiver might or could do, but shall be liable for all costs accrued and to accrue in case of an unsuccessful issue.

SECTION 19. *Compromise of debt or claim.*—An assignee or receiver may compound or compromise any debt or claim due to the insolvent, if done in good faith and after proper inquiry; and, upon payment of the amount due, may require all mortgages, conditional contracts, pledges and liens, of or upon any real or personal property of the insolvent, to be satisfied, cancelled or assigned to him, as he may deem best, or he may sell the property subject thereto. Where any realty

is subject to liens or claims which, under existing laws would be discharged by a judicial sale, such liens and claims shall be unaffected by a private sale of such realty; but a public sale may be made thereof, freed and clear of such liens or claims, by leave of court, after notice to the claimants; and the fund realized shall take the place of the liens or claims, and be distributed on the settlement of the account of the assignee or receiver, to the parties found entitled thereto. Executions issued on such liens or claims may be stayed by the court, to enable the property to be sold by the assignee or receiver. If a creditor purchases property upon which he has a lien or claim, he shall, after payment to the assignee or receiver of all the costs and expenses of the sale, and the amount of all prior liens or claims discharged by the sale, if any, be entitled to receipt to the assignee or receiver to the extent of his lien or claim, upon giving security, to be approved by the court, conditioned to make good the amount receipted for if it shall afterwards be made to appear that, for any cause, he should not be allowed such preference.

SECTION 20. *Purchase by assignee.*—No assignee or receiver shall purchase, directly or indirectly, any part of the assets of such insolvent except by leave of court, after notice to all the known creditors; nor shall he employ any person as manager or attorney who is related to the assignor, or has any interest, individually or as attorney, for any particular creditor, or in opposition to an equal distribution of the whole of the assignor's estate among all his creditors.

SECTION 21. *Deposit of money.*—The assignee or receiver shall as soon as may be after receiving any money belonging to the estate, deposit the same in some bank or trust company in good standing, in his name as assignee or receiver, and shall, as far as practicable keep all the assets of said estate separate and apart from his own, or designated by appropriate marks, so that they may be easily and clearly distinguished as the property of the insolvent's estate.

SECTION 22. *Notice to creditors.*—The assignees immediately after the meeting of the creditors aforesaid, and the receivers immediately after their appointment, shall give

written or printed notice to all the creditors known to them, requiring such creditors, within six months from the date of such notice, to make proof of their claims in the manner hereinafter set forth, or be debarred from coming in upon the fund. They shall also, at the same time, advertise such notice in one daily newspaper in said county, and in such legal periodical, if any, as shall be designated by the court, once a week for four successive weeks.

SECTION 23. *Form of affidavit of claim.*—No claim against the insolvent's estate shall be allowed unless the claimant, or some one for him if he cannot do so, shall furnish to the assignee or receiver a statement of his claim, together with a copy of any book entries appertaining thereto, or any note or other writing evidencing the same, verified by an affidavit in the following form:

I, G. H., do solemnly swear (or affirm) that the above is a true statement of my claim against the insolvent estate of E. F.; that there are no credits or allowances thereagainst, except as therein set forth; that I have not directly or indirectly made or entered into any bargain, arrangement or agreement, express or implied, to take or receive, directly or indirectly, any money, property, or consideration whatever, to or for myself, or to or for any other person, firm or corporation whatsoever, other than my dividend as a creditor of said estate, and that there is no collateral security for said indebtedness, or any part thereof, held by me or anyone else, other than as above set forth. So help me God (or, and so I do affirm).

If such claim and affidavit be in proper form, and the balance claimed agrees with the amount stated by the insolvent, or upon consultation between the creditor and the insolvent the amount is agreed upon, the claim shall be allowed if presented before the filing or audit of the account, unless objected to in the manner hereinafter set forth.

SECTION 24. *Filing of account.*—As soon after the expiration of said year as the assets shall have been collected, or whensoever thereafter required by the court, the assignee or receiver shall file his account, and a list of the claims proven before him, in the proper court, duly sworn to by him as correct

in all particulars; and if there are no claims remaining unadjusted, he shall give a written or printed notice to the insolvent and all the creditors known to him, in the following form:

You are hereby notified that my account and a list of the claims proved before me has been filed in the Court of Common Pleas of _____ county, as of _____ Term, eighteen hundred and _____ Number _____, and that said account will be allowed and distribution of the balance shown thereby will be made among the creditors therein named, according to their respective claims, on _____, the _____ day of _____, eighteen hundred and _____, unless objections be filed thereto or to any of said claims, before that time.

SECTION 25. *Advertisement. Confirmation of account. Distribution.*—The time fixed in said notice shall be between three and five weeks distant from the date thereof; and if there shall be unrepresented creditors, whose addresses are unknown, an advertisement thereof shall be inserted in one newspaper, published in the county, and in the legal periodical, if any, designated by the court, once a week for three successive weeks, prior to the time of meeting. On the date fixed, if no objections have been filed, the account shall be confirmed absolutely; the assignee or receiver shall prepare a schedule of distribution, which shall be approved and filed, and shall distribute the assets in his hands in accordance therewith.

SECTION 26. *Auditor. Form of notice.*—If at the time of filing the account and list of proved claims, there are claims which remain unadjusted, or if objections be filed, the court shall hear and decide the disputed matters, or, in its discretion, may appoint an auditor for that purpose. The court or the auditor shall fix a time and place for the hearing, of which three weeks' notice shall be given by the assignee or receiver to the insolvent and all the creditors known to him, in the following form:

You are hereby notified that the court will (or, I. J. has been appointed auditor to) audit, settle and adjust my account as assignee (or receiver) of the estate of E. F., an insolvent, and make distribution among the creditors of said estate, and that a meeting for that purpose will be held at

in the of , on the day
 of , eighteen hundred and , when and where
 you may be heard if you so desire.

If there shall have been no advertisement of the filing of the account, said notice shall be advertised, also in one newspaper published in the county, and in the legal periodical, if any, designated by the court, once a week for three successive weeks, prior to the meeting.

SECTION 27. *Objections to claim.*—The hearing before the court or auditor, in case of objections filed, shall be confined thereto, unless the court, upon cause shown, shall give leave to file other objections. If objections be made to any claim duly verified, as aforesaid, whether upon objections filed or otherwise, express notice and an opportunity to defend the same shall be given to such creditor. The costs before the court or auditor shall be charged upon the fund or against any party appearing, according to equitable principles.

SECTION 28. *Date of claims. Primary and secondary liability. Collateral security.*—All claims shall be made as of the date of the distribution of the fund, interest being allowed or discount being made to that time. A creditor having a claim for which the insolvent is primarily liable, and others secondarily, may prove for his whole claim; but, if the insolvent is only secondarily liable, the value of the liability of the primary debtor shall be adjusted between the creditor and the assignee; or, if the valuation cannot be agreed on, the same shall be submitted to the appropriate tribunal, and a dividend shall only be awarded to the creditor on the difference between such value, so determined, and the amount of his claim. In like manner, any collateral security held by any creditor for his debt shall be valued by said tribunal, and if the security be retained by the creditor his dividend shall be on the difference between his claim and the value of his security, so ascertained: Provided, That the creditor shall have the right to surrender his security, and take a dividend on his whole debt. If such creditor refuses to have his security valued or surrender the same, he shall be excluded from participation in the fund.

SECTION 29. *Fraud and collusion.*—Any creditor who

shall, upon such distribution, present a claim, whether in judgment or otherwise, which shall be so largely in excess of that which is actually due as to be fraudulent and collusive, or shall assist others in so doing; or shall collude with the insolvent to hinder, delay or defraud his creditors, or any of them; or shall have received a preference from the insolvent, in violation of the provisions of this act, and shall not voluntarily surrender the same to the assignee or receiver, shall be postponed to all other creditors on the distribution of the insolvent's estate.

SECTION 30. *Form of triplicate release.*—At the time of receiving his dividend in case of a voluntary assignment, each creditor shall sign triplicate releases in the following form:

The undersigned creditors of E. F., an insolvent, for and in consideration of the sums of money set opposite our respective names, and received by us from A. B., assignee of the estate of E. F., an insolvent, do hereby release the said E. F. from any and every debt, demand and liability which we had or may have had against him, at the date of his assignment, on the day of , Anno Domini eighteen hundred and , whether due or not; and hereby agree that no suit, action or execution shall be maintained for or by reason of such debt, demand, or liability, reserving, however, to ourselves the right to avoid this release, upon showing any of the matters or things which, under the insolvent laws, shall entitle us to retain our respective claims against said insolvent, notwithstanding our participation in the settlement of his estate.

Witness our hands, the dates set opposite our respective names.

One of said releases shall be filed in court, one shall be retained by the assignee, and one shall be delivered to the insolvent.

SECTION 31. *Exemption.*—An insolvent shall be entitled to the same exemption out of the assigned estate as he would be had an execution been issued against him; and his right thereto shall not be denied for or by reason of the character of any claim presented, or by reason of any waiver in any

contract or judgment, or by reason of failure to reserve it in the deed of assignment. Any lien or claim for wages, for rent, of mechanics and material men, or otherwise, which by virtue of any act of Assembly would be preferred in case of an execution, shall retain its preference in case of an assignment, and to the same extent. Rent accruing after the date of the assignment, and wages necessarily incurred in service rendered to or for the assignee or receiver, shall be paid as part of the expenses appertaining to the assignment. Except as herein otherwise provided, all and every interest, claim and estate in the property shall be discharged or divested by an assignee's or receiver's sale, if it would have been discharged or divested by a sale under an execution at the time of the assignment, and not otherwise.

SECTION 32. *Secreted property.*—Any person who shall discover to the assignee or receiver any secreted property, real or personal, in the possession or control of a third party, and in which the insolvent estate has an interest, shall receive out of the proceeds thereof, for so doing, an amount, to be fixed by the court or auditor, at least equal to the commission of the assignee or receiver in regard thereto.

SECTION 33. *Discharge from liability.*—Nothing in this act shall be taken or understood as discharging an insolvent from liability to such of his creditors as do not choose to exhibit their claims, or who, before the schedule of distribution is made or filed, withdraw their claims; but, with respect to creditors who exhibit their claims before a voluntary assignee, or an auditor appointed in such case, and do not withdraw them as aforesaid, they shall be wholly debarred from maintaining afterwards, by suit, action, execution or otherwise, any claim existing at the time of the assignment, whether due or not, unless he shall aver and prove:

(1) That said action is founded on the actual force, fraud, malice, or deceit of the insolvent; or,

(2) That said action is founded on the embezzlement or malfeasance of the insolvent; or, for libel, slander, malicious prosecution, conspiracy, seduction or criminal conversation; or,

(3) That such action is founded on the purchase by the insolvent of real or personal property, on credit and without security therefor, when he had reasonable cause to believe that he would not be able to pay therefor; or,

(4) That such insolvent has wilfully sworn falsely in any material fact appertaining to the settlement of his estate, or has failed and refused to make all necessary conveyances to enable the assignee to speedily and effectively settle the same; or,

(5) That such insolvent fraudulently secreted, altered, injured, defaced or destroyed any part of his estate; or any books, documents, muniments of title, or writings appertaining thereto, or permitted the same to be done; or has secreted, conveyed or incumbered any part of his property, for the benefit of himself or family; or has collected and retained any of the assets of the assigned estate; or, in contemplation of insolvency, has failed to keep the books of accounts and papers usually kept by him in his business; or,

(6) That such insolvent has made any promise of future advantage to any creditor, or has knowingly permitted others to do so, to induce any creditor to participate in the settlement of the assigned estate, and has failed to disclose the same to the complaining creditor; or,

(7) That such insolvent, while knowingly insolvent or in contemplation of insolvency, has in any manner preferred or attempted to prefer one creditor to another, or permitted such preference to be obtained by judgment, execution, attachment, sequestration, or otherwise; or,

(8) That such insolvent has knowingly permitted a false or exaggerated claim to be made against said estate; or,

(9) That such insolvent has absented himself or concealed his property, to avoid an execution; or,

(10) That the insolvency arose from losses by gambling, or in the purchase of lottery tickets; or,

(11) That such insolvent has previously been an insolvent, and obtained a release of his debts under the provisions of the insolvent laws.

But the benefits of this section shall not apply in favor

of any insolvent who was forced into the hands of a receiver by the action of his creditors.

SECTION 34. *Release of persons secondarily liable.*—In cases where the insolvent is primarily liable for a claim proved against his estate, a discharge of that liability, by the creditor accepting a dividend under this act, shall not operate to release or discharge any person secondarily liable for the same debt, contract, engagement or other liability, if the participating creditor shall have given such third party written notice and an opportunity to purchase the claim and subrogate himself to the rights of such creditor; but, in that event, such secondary liability shall remain, in like manner as if such discharge had not taken place; but, if the creditor does not give such notice, the discharge of the insolvent from primary liability shall also operate to discharge from liability the party secondarily liable.

SECTION 35.—*Order of court for seven years' exemption.*—Whenever a majority in number and value of the creditors of an insolvent, who has made a voluntary assignment for the benefit of his creditors, shall consent in writing thereto, it shall be lawful for the court, upon application of such debtor, and notice thereof given to all undischarged creditors, in the manner hereinbefore provided for giving notice of the meeting of creditors, to make an order that the estate and effects which such insolvent may afterwards acquire shall be exempted, for the term of seven years thereafter, from execution, for any debt contracted or cause of action existing previously to such assignment; and if, after such order and consent, any execution shall be issued for such debt or cause of action, it shall be the duty of any judge of the court from which such execution issued to set aside the same, with costs.

SECTION 36. *Restoration of estate not sold.*—If any such insolvent or his legal representative shall satisfy the undisputed claims of his creditors, and shall give security, to be approved by the court, to pay those which are disputed, the court shall order his estate and effects, not sold, to be restored to him or his legal representatives; and he shall, by virtue of such order, be seized and possessed thereof as of his former

estate and title thereto; and if, upon the final settlement of accounts by the assignee or receiver, there shall be a surplus, after payment of all the claims presented and allowed, the same shall be paid to such insolvent or his legal representatives.

SECTION 37. *Removal of assignee or receiver.*—Any creditor may, by petition, move the court to discharge any assignee or receiver for dereliction of duty, incompetency or other reason affecting the estate; or the assignee or receiver may voluntarily petition for his own discharge; and if the court shall be of the opinion that the interests of the estate will be conserved by the appointment of some other person in his place or stead, it shall grant the prayer of such petition, and appoint a new assignee or receiver, with like powers and duties as the one removed, upon entering security as in the case of the original assignee; but such removal shall be without prejudice to all claims upon said assignee or receiver and their securities, growing out of their performance or non-performance of duty. The assignee or receiver thus removed shall remain under control of the court, for the purpose of compelling him to make all necessary transfers of the assets of the insolvent estate to his successor or any others interested therein, or to give needed information and assistance in the settlement of the estate. If the assignee removed be the one selected by the creditors, the new appointee shall be selected in like manner.

SECTION 38. *In case of vacancy.*—Any creditor may, in case of a vacancy in the office of assignee or receiver, petition the court for the appointment of a new assignee, whenever he may have reason to believe that there are assets of the assigned estate that have not yet been collected, or that any duties appertaining to the office remain unperformed; and such appointment shall be made by the court with the same effect as in a case of the original appointment.

SECTION 39. *Appeal.*—Any final judgment, order or decree, or any order or decree resulting in imprisonment, made under the provisions of this act, may be appealed from to the Supreme or Superior Court, as in other cases.

SECTION 40. *Perjury.*—If any insolvent shall be con-

victed of perjury, in respect to any oath or affirmation taken by virtue of this act, he shall be liable to arrest and committal on mesne process, and to be charged in execution, in the same manner as if he had not before been arrested or taken in execution, or as if he had not made application for the benefit of the insolvent laws; and, moreover, such person shall never afterwards be entitled to his discharge as an insolvent debtor by virtue of this act.

SECTION 41. *Definition of an insolvent.*—A person shall be deemed insolvent, within the provisions of this act, whenever the aggregate of his property, exclusive of any property which he may have conveyed, transferred, concealed or removed, or permitted to be concealed or removed, with intent to defraud, hinder or delay his creditors, shall not at a fair valuation be sufficient in amount to pay his debts.

The statute of May 3, 1905, provides that when an assignment has been made for the benefit of creditors, in another state, and an estate or interest in real property or lands in this state has been heretofore vested or shall hereafter vest in the assignee or other trustee under said assignment, the trust shall cease at the expiration of twenty-five years from the time when the trust was created, except where a shorter limitation is contained in the instrument creating the trust; and the estate or interest in the real property or lands in this state, remaining in the trustee or assignee, shall thereupon revert to the assignor, or to his heirs or assigns, as if the trust had not been created.

BOOK SECOND

AGENCY, PARTNERSHIPS AND CORPORATIONS

PART I AGENCY

CHAPTER XVIII.

THE FORMATION OF AGENCY.

An agent is defined as one who acts for another, called the principal. If the agent is employed by the principal in accordance with an agreement between them, we need not inquire into the method by which the employment contract is made. The rules about the formation of contracts in general apply to contracts of employment. Most employment contracts require no special formality, but we should recall what was said at the close of the seventh chapter about apprenticeship contracts. We may, then, pass over the subject of forming a contract between principal and agent which will bind these two parties. It *particularly concerns us* in the present chapter *to see how the relation of principal and agent may be formed, so as to make the principal liable to third parties for acts of the agent*. Agency may be created in one of four ways: first, by express agreement; second, by appointment; third, by estoppel; and, fourth, by ratification.

(A) Agency created by express agreement.

This is the simplest method by which a principal may appoint an agent. Such express agreement is a contract, if it has the necessary elements. It is not necessary, however, as against third persons that there should be a binding contract of employment between the principal and the agent. For instance, suppose the agent is to get no consideration for his work. If he goes ahead anyway, and proceeds to make a contract on behalf of his principal with a third person, the contract is binding, if the agent acted within his authority. Again, suppose that the agent is only eighteen years old, and that he is authorized by his principal, who is over age, to make a contract with a third person, who is also over age. The mere fact that the agent's contract of employment is voidable does not invalidate the contract between his principal and the third party. To this second contract the agent is no party, for he is merely the instrument whereby his principal forms the contract.

You will recollect from what was said about contracts that a contract of employment does not usually need to be in writing. One exception to this rule occurs where the agent represents his principal in certain real estate contracts, as appears from what is said in the seventh chapter about the act of 1772. While, however, no writing is legally required by most agents, there are many cases in which it is practically necessary. If the principal is at a distance, third persons may refuse to recognize the agent, unless he produces a writing, called a power of attorney, to establish his authority. This is useful for the protection of the agent himself, because we shall see that he may incur serious responsibility if he cannot prove that he really has authority to represent his principal. It is often wise to have a power of attorney acknowledged before a notary, and this is usually necessary if the agent is to sign a deed or mortgage for his principal.

(B) Agency created by appointment.

The third rule about offer and acceptance in the second chapter shows that a contract may be made either by words or by conduct. Likewise, an agent may derive his authority, not from any express words, written or unwritten, but from the fact that he has been appointed to a certain position. When the holding of a position entails certain duties upon the man who lawfully occupies it, naturally he is endowed with such authority as is needed to fulfil those duties. If, for instance, a railroad company raises an employee to the position of freight claim agent, it becomes his duty to adjust claims arising out of the delay and destruction of freight. Suppose that former freight claim agents have always exercised certain powers in settling such claims, and the newcomer makes an adjustment which is in accordance with what he has often seen done when he was a subordinate in the same department. The railroad company could not deny his authority, even though it had not been expressly conferred upon him. It went with the appointment.

(C) Agency created by estoppel.

When considering the contractual powers of minors in the fourth chapter, we saw about the case of *Logan v. Gardner*, where one of the many phases of estoppel was considered. It was stated that the doctrine of estoppel is often applied when a person has helped to mislead others to their disadvantage, and afterwards attempts to assert rights against them which are inconsistent with the position which the same person formerly pretended or at least seemed to occupy. This situation arises when a person has allowed another to pose as his agent, and, after thus helping to mislead others, seeks to repudiate the alleged agent. An example of this is presented in the case of *Williams v. Getty* (1858), 31 Pa. 461. Williams was a railroad contractor, who employed John O'Leary as his general manager. O'Leary made a contract with Getty, whereby the latter was to supply a team and driver for several months. After a few weeks O'Leary discharged the driver without just

cause, and Getty could not find employment for the team and his man for some time. He sued Williams to recover damages for the breach of contract, and Williams defended on the ground that O'Leary had no authority to make a long term contract. The court decided in Getty's favor, saying, "If the principal holds the agent out to the world as a general agent, in the transaction of his business, any contract made by the agent within the scope of that business would be binding on the principal, although there might be, as between the principal and agent, a restriction upon the latter's authority, if the person with whom the contract was made had no notice of such restriction." By clothing O'Leary with the appearances of full authority to represent him, Williams precluded, or "estopped," himself from denying the authority, as against an innocent person who was misled by appearances.

Even where a person who calls himself another's agent has never been given the least trace of authority, he may bind his alleged principal, if the latter tacitly acquiesces in the falsehood. If a man goes about stating that he represents you, and people make agreements with him on the strength of what he tells them, they cannot hold you liable unless you have contributed to the fraud. The principal's liability in a case of agency by estoppel is based not so much on the acts of the alleged agent, as on the fact that the alleged principal has been guilty of fraud or negligence in knowingly allowing the agent to seem to have more authority than he actually possesses. When an agent has been discharged it is often wise to notify those with whom he has been dealing for the principal, because he may continue to visit the same people, and pretend that he still represents his old employer. Thus, if you dismiss a man who has been collecting rents for you, it is often advisable to notify your tenants at once that they must pay nothing to him in the future.

(D) Agency created by ratification.

Suppose that a man who pretends to be another's agent has never been given authority either by express agreement or by appointment, and that the alleged principal is not liable

through the doctrine of estoppel, because he has never held the agent out to the world as his representative. Suppose a third person trusts solely to the agent's statement that he represents the alleged principal. When the latter learns about what has been done, he may repudiate it, and refuse to be bound by the act of one to whom he has not given authority. On the other hand, he may choose to adopt what has been done, and ratify the agent's act. Indeed, if he fails to repudiate it, after learning of what the alleged agent has done, the courts will ordinarily consider that he has decided to ratify it, if the rights of third persons are affected. Even as between the principal and agent, the former's failure to disavow the latter's acts may sometimes amount to ratification. For instance, in the case of *Geyer v. Decker* (1795), 1 Yeates 486, it appeared that Geyer had shipped seven casks of liquor to Decker with instructions to sell them and remit the proceeds in bank notes. Decker sold some of the goods on credit, and remitted what money he had received, less his commissions. He had previously informed Geyer that it was hard to sell for cash. After a long delay Geyer sued Decker for the balance remaining due by those to whom the latter had given credit. The court decided that Geyer had ratified the giving of credit by his failure to object to it sooner. The law books are full of cases showing how dangerous it is to be slothful in asserting your rights. On ratification, see *McClintock v. Oil Co.* (1892), 146 Pa. 144.

CHAPTER XIX.

THE TERMINATION OF AGENCY.

As between the principal and the agent, where there has been a contract of employment, the termination of that contract is subject to the same rules that are laid down in the fourth part of the preceding book. There we saw about the discharge of contracts in general, and a question about the discharge of any particular contract falls under the same broad principles. Since, however, the fact that an agent frequently

deals with *third parties* complicates the situation, there are some new points to be treated in this chapter.

What will be said about the termination of agency relates to cases where there is no contract of employment, as well as to cases in which the agent is regularly hired under a contract and receives consideration for his services. We are studying mainly the question as to the termination of his power to bind the principal by acts which he may do as the latter's representative. The agency relation may be terminated, just as contracts may be discharged, in any one of the five following ways: first, by agreement; second, by performance; third, by breach; fourth, by impossibility; and, fifth, by bankruptcy.

(A) *Termination of agency by agreement.*

The principal and the agent are free to part company and to cancel existing arrangements at any time, even though they have agreed to continue relations with each other for a much longer period. Most of what is said on the subject of discharge of contracts by agreement is applicable here also. If the principal has given the agent any writing which indicates that the latter's authority is to continue for a long period, he should try to get this back. If there is any fear lest the agent should continue to deal with third persons, on behalf of his former principal, pretending still to have authority, the principal should be especially careful to notify third persons with whom the agent has been acting for him in the past.

Where no time has been fixed for the duration of the employment, usually either party is free to terminate it at once by so notifying the other. An example of this rule is found in *Hill v. Jones* (1893), 152 Pa. 433. Hill, a real estate broker, agreed to sell a tract of land belonging to Jones, which had been laid out in 449 building lots. He was to get \$10 for the sale of each lot. He put up a temporary office on the land, and incurred expenses amounting to \$233. After he had sold two lots, it was found that a good title could not be conveyed, because the wife of Jones refused to sign the deeds. Jones notified Hill that he was unable to carry out the agree-

ment, and Hill sued him for \$4,490. The court held that Hill's authority might be revoked at any time by Jones. Hill was allowed to recover \$233, because it was unfair to make him bear the expenses incurred in connection with the agency. He had laid out this sum on the supposition that Jones would not suddenly revoke his authority before he should get a reasonable chance to profit by it.

(B) *Termination of agency by performance.*

If the agent has been engaged for a certain piece of work alone, the conclusion of that work naturally terminates the agency. Again, if he has been employed for a limited period, when that period expires the relation between the parties is at an end, unless they agree to renew it. The mere fact that the agent has not been fully paid for his services will rarely continue his authority in existence after the expiration of the time to which it has been limited.

(C) *Termination of agency by breach.*

The principal may deprive the agent of authority at any time, even though he has agreed in the contract of employment that the agent shall continue in his service for a much longer period, and even though the agent has given no cause for complaint. This rule may seem in conflict with the principle which forbids the obligation of a contract to be impaired. The difficulty may be explained by distinguishing between the *power* which the agent acquires under the contract of employment, and the *rights* which he bargains for in the same contract. He is protected in the enjoyment of his contractual rights. Usually the most valuable right that he gets is the right to receive compensation for his work, and if he is unjustly discharged, the courts will compel his employer to make good his loss. The power or authority which comes to him in connection with the employment is usually not secured to him by contract. It is merely something which incidentally pertains to the discharge of his duties. While, therefore, the em-

ployer cannot take away his agent's contractual right to compensation, he can deprive the agent of power to represent him, and the agent should not attempt to act after being notified not to do so. If the unjust deprivation of authority prevents the agent from doing his work, he may claim compensation for what work he could have done, if the principal had permitted him to go ahead as agreed.

An *exception* to the foregoing rule occurs where the agent receives authority, not in order to further the principal's interests, but rather for the benefit of himself or some third person. *Judgment notes* usually contain a clause authorizing either some named lawyer or any lawyer to appear in court on behalf of the person who signs the note, and confess judgment for him. This dangerous clause in the judgment note is not inserted for the maker's benefit, but for the benefit of the holder of the note. Suppose you borrow money on a judgment note, and afterwards become afraid that if it is entered up in court your credit will be injured. You have no right to revoke the agency which you created when you signed the note. The power given to any lawyer who may enter it up as your representative was "*coupled with an interest.*" In this exceptional case the holder of the note has a contractual right to retain in full force the power of attorney which you signed. Again, suppose you have a certificate for thirty shares of stock in the United States Steel Corporation, and borrow \$600 on it from a bank. You sign a blank power of attorney authorizing any person whose name may be filled in later to have the certificate transferred out of your name on the stock books of the Steel Corporation. You could not revoke the authority so given by you without repaying the loan, because the bank has a contractual right to keep the power of attorney for use in an emergency, and for helping to secure the repayment of its money.

(D) *Termination of agency by impossibility.*

The only way in which the agency is likely to be terminated under this heading occurs when the principal or the agent dies, or becomes unable to continue the agency relation

through bodily or mental weakness. Obviously, when the agent dies or becomes permanently disabled he can no longer act for the principal. Where the agent has been authorized to appoint a *sub-agent*, the latter's authority usually ceases upon the death of the main agent, because it is derived from him. The death of the principal also terminates the agent's authority except in some cases where it is "coupled with an interest," as explained in the preceding paragraph. In the case of the loan by a bank on the security of Steel Corporation stock, the power of attorney given to the bank is not revoked by the borrower's death. In the case of judgment notes, however, the power of attorney dies with the one who gave it. If the note has not been entered up in the prothonotary's office before the maker's death, the power of attorney is of no use. One reason for this is that the standing of the persons interested in the estate of the deceased principal is fixed at the moment of his death. Thereafter nobody save an executor or administrator should assume to act as his representative. The courts are, however, disposed to protect an agent who enters into contracts on behalf of his deceased principal before he learns about the latter's death, and also to protect an innocent third party under such circumstances.

(E) *Termination of agency by bankruptcy.*

The principal's bankruptcy terminates the agency. The agent's bankruptcy often has the same effect. The more responsible the agent's position, the more likely will his bankruptcy bring the agency relation to an end.

CHAPTER XX.

THE RIGHTS AND OBLIGATIONS OF PRINCIPALS, AGENTS AND THIRD PARTIES.

We know that a legal right acquired by one party under a contract exactly matches the legal obligation which the other party assumes. It would be useless, therefore, to consider, say, the obligations due by an agent to his principal, and

afterwards to consider the rights of a principal as against his agent. It will suffice then to speak merely about the *obligations* which are incurred by principals, agents and third parties. These may be divided into six classes: first, obligations of the agent towards his principal; second, obligations of the agent towards third parties; third, obligations of the principal towards his agent; fourth, obligations of the principal towards third parties; fifth, obligations of third parties towards the principal; and, sixth, obligations of third parties towards the agent.

(A) *The agent's obligations towards his principal.*

Where the agent enters into a contract of employment with his principal, the terms of the contract, of course, govern him. The confidential relation of principal and agent, however, imposes a *special obligation* on the latter, although the contract is silent about it. This obligation extends even to agents who get no consideration, and who do not make a contract with their principals. The agent is bound by the nature of his position to be *loyal* to his principal. He should not represent both parties to a contract, without letting each know that he also represents the other. A man cannot serve two masters. If an agent, for instance, represents both the seller and the purchaser in a contract of sale, without telling them of the fact, he is not entitled to commissions from either. Indeed, such a contract would be voidable, perhaps, at the instance of either party, if he took prompt steps to set it aside on first learning that his agent also represented the other party, and if no harm would be done by nullifying it.

What has just been said shows that an agent who has been employed, for instance, to sell a house must not buy it himself without mentioning the fact to his principal. The agent will be strongly tempted to get the lowest price for himself, and this is in direct conflict with his duty to his principal. The principal may usually have such a contract set aside, although no fraud was intended and no injury done. This rule applies to executors, administrators, guardians,

attorneys-at-law, general and special agents, and all persons who have any concern in the sale of another's property. It extends to all kinds of public sales as well as to private sales. An agent must not take secret rebates, and should usually give his principal the benefit of whatever may come to him in the course of his work. This was decided in the case of *Storing Co. v. Pentecost* (1875), 79 Pa. 491. Pentecost sued for commissions on the sale of real estate, as well as for printing and other expenses. At the trial he admitted on cross-examination that he charged the storing company the ordinary printing rates, although he received a discount of 25 per cent on account of the large amount of business which he did with the printer. The court held him bound to give the storing company the benefit of this discount, for it was his duty to procure the advertising on the best possible terms for his principal. See also *Wilkinson v. McCullough* (1900), 196 Pa. 205.

An agent should strictly follow instructions, and if he departs from them he is liable for the consequences, even though he acts in good faith. He is safe as long as he obeys instructions, and remains faithful and diligent. He should keep his principal informed of matters which it may be important for the latter to know. A sub-agent, however, is bound only to notify the agent who is over him. *An agent is not presumed to guarantee the success of whatever he does*, unless he expressly undertakes this heavy liability. Most salesmen who are authorized by their principals to sell on credit are not responsible if the purchasers fail to pay, although any salesman who takes it on himself to sell on credit to a person known to be insolvent, violates the primary duty of fidelity to his employer, and is responsible.

Where you employ a person in a professional capacity, or anyone who holds himself out as possessing a certain degree of skill you are justified in expecting that he will serve you not only with fidelity, but also with such ability as is ordinarily found in persons pursuing the same profession or business. For instance, if you employ a dentist, who does the best he can for you, but displays ignorance of matters which the average dentist is thoroughly versed in, you may recover damages from him for the resulting harm,

(B) *The agent's obligations towards third parties.*

The agent should try to avoid all liability to third parties. If he exceeds his authority, and third parties are, therefore, unable to hold the principal upon the contract which the agent assumes to make, the agent himself may be made responsible. He cannot escape personal liability merely by proving that he did not know that he was overstepping his power. In order to avoid this danger, the agent should get explicit directions as to his duties, preferably in writing. An agent is usually liable personally for the *torts* and *crimes* which he commits in the service of his principal, for he should not be allowed to shield himself from the consequences of wrongdoing, even though he acted in another's interest.

Where an agent is acting for another, but fails to disclose this fact to the third party with whom he deals, he is personally liable. Even where the third party knows about his principal, an agent should be careful to sign contracts with the principal's name, rather than with his own. This is especially true of negotiable contracts. For instance, if James Lord is agent for John Green, he should sign contracts as follows: "John Green, per James Lord, Agent." He should beware of signing contracts as follows: "James Lord, Agent." In the case of *Barclay v. Pursley* (1885), 110 Pa. 13, the court was called on to consider a check signed as follows: "David Pursley, Fr." Pursley was sued personally on this check, but contended that Barclay understood that it was intended as the check of John Ardell, Pursley's employer. The court held that he would be excused from liability if his contention were proved, but intimated that Pursley had attempted very awkwardly to qualify his personal liability by adding the letters "Fr." after his signature. He swore that these letters stood for the word "foreman," and that Ardell had employed him in that capacity. In many other cases careless agents have subjected themselves to even greater trouble than in Pursley's case by signing contracts in some irregular way. See Section 20 and Section 69 of the negotiable instruments act in the tenth chapter.

(C) The principal's obligations towards his agent.

The principal is bound to pay the agent compensation, where there is a contract between them which so provides either expressly or impliedly. He is given a wide discretion in directing how the agent shall work for him, but he cannot entirely change the nature of the agent's employment, even though he is willing to pay the same wages. For instance, if he employs a man as a buyer of linen, he has a right to reduce the buyer's authority by employing another linen buyer, and giving each of them charge of certain kinds of goods. He would have no right to degrade the buyer, as, for instance, by setting him to work in the capacity of a floor-sweeper.

Where employees work in a store, factory, mine, or other place of business conducted by their employer, the latter is bound to make it reasonably safe for them. Some occupations are naturally dangerous, but the employer does not by any means insure the safety of his workmen. Where employees are young or inexperienced, their master should provide them with suitable instruction. If the employer is careful in the selection of a certain workman, who afterwards negligently injures a fellow-workman, the latter has no right of action against the employer. So far as employees are concerned the employer is only responsible for injuries caused by his own personal negligence, or by that of any persons whom he puts in charge of his establishment. If the manager of a large mill, for instance, is negligent in inspecting the floors of the mill, and one of the floors finally falls down, injuring an employee below, the principal is responsible for the conduct of the manager. The latter is called a vice-principal, and if an ordinary inspection by him would have revealed the condition of the floor, the proprietor of the mill is liable. Even though the vice-principal or the employer himself is negligent, the latter cannot be held liable if the employee was sufficiently capable of understanding the danger he was under, and assumed the risk. Likewise, an employer cannot be held liable if the employee's own negligence contributed to cause the accident. The employee in the case just mentioned would be

guilty of contributory negligence if he had selected a place for running a machine in his charge quite close to the prop which sustained the floor above, knowing that the proximity of this machine to the prop caused the latter to vibrate and become loose. We shall see in a subsequent paragraph that the employer is responsible for injuries caused to third parties by the negligence not only of his vice-principal, but also of many other agents.

An apprentice has a right to receive instruction in the trade or occupation for which he is bound out. His master should also see that he gets a reasonable general education, if he does not possess it when the apprenticeship contract is made. The act of May 2, 1905, forbids the employment of children under fourteen in any factory, manufacturing or mercantile industry, or other establishment except those employing domestic, coal-mining or farm labor. It also forbids anyone under sixteen years to be so employed unless a certificate made out in accordance with the terms of the act is filed with the employer. The provisions of the act relating to certificates have been held invalid. In the case of *Collett v. Scott* (1906), 30 Super. 430, it was held that similar provisions in the anthracite mine-laborers act of 1905, are in conflict with the United States Constitution. The industrial act of May 2, 1905, also forbids the employment of any male minor under sixteen or of a female of any age in the establishments mentioned above for a longer period than twelve hours in any day, or for a longer period than sixty hours in any week, except in the case of retail mercantile establishments for twenty days before Christmas. The act also regulates the employment of those under sixteen at night work. The same act provides for the guarding of dangerous machinery, and forbids minors under sixteen to be allowed to clean or oil machinery while it is in motion, or to be put in charge of elevators. The act defines the duties of certain classes of employers in many other respects and provides for the comfort of their employees. The acts of April 11, 1895, and May 5, 1897, prohibit sweat-shops, directing that no room or apartment in any tenement or dwelling house shall be used for the manufacture of certain goods, except by the

immediate members of the family living therein, or by the family seamstress. The employment act of May 2, 1905, deals with this matter also. On the same day, May 2, 1905, the act concerning anthracite coal-miners, referred to above, was passed by the legislature. The employment of bituminous coal-miners is also regulated by statute. See the acts of May 15, 1893; June 2, 1891, and May 13, 1903, which relate to mining.

If an employee is unable to work through sickness for a short time, this does not usually discharge the contract, but the employer is not bound to pay him for the lost time. If the employee is permanently disabled, he may recover the wages which he has already earned, but the contract is discharged by impossibility, as mentioned in the sixteenth chapter.

Returning to the consideration of agents who are authorized to transact business with third persons, and who, therefore, may be said to represent their principals to a greater degree than the ordinary workman, we should note that the agent is sometimes entitled to more than the wages or salary which he was to get under the contract. If he is compelled to pay money out of his own pocket as a result of what he does to advance his principal's interests, the latter must reimburse him. This appears from the case of *Abraham v. Mitchell* (1886), 112 Pa. 230. Abraham sold lumber for Mitchell. The purchaser partly paid for it with a note at four months, which was payable to Abraham's order. Abraham said that the note should have been made payable to Mitchell, but the purchaser objected because the account on his books had been put in Abraham's name. Abraham handed the note to Mitchell, indorsing it in order that the latter might raise money on it. The note was discounted, but was not paid at maturity, and Abraham, being the first indorser, had to make it good. He tried to collect the money from the maker of the note, and failing in this sued Mitchell. The court decided that under this state of facts, Mitchell should pay the amount of the note, for the indorsement had been made entirely for his benefit.

(D) *The principal's obligations towards third parties.*

Under the heading Creation of Agency by Estoppel, it was pointed out that a principal is liable for what his agent does not only within the real scope, but also within the apparent scope of his authority. If, however, the principal has not known that his agent was violating instructions, and has contributed in no way to mislead third persons, he is not liable for the agent's unauthorized acts. A third person who deals with an alleged agent, and who fails to consult the principal, usually takes the risk of learning afterwards to his cost that the self-styled agent has been acting without authority. Some of the troubles which face a third party who does not make sure of an alleged agent's authority are shown in the case of *American Underwriters' Association v. George* (1881), 97 Pa. 238. George sued on a fire insurance policy covering certain property in Texas which had been burned. The policy had been issued by John E. Barry, and George offered in evidence an agreement between Barry and Angomar & Co., which recited that Barry was authorized to issue policies for the Underwriters' Association. The jury decided in George's favor, but the Supreme Court set the verdict aside on several grounds. George had taken it for granted that Angomar & Co. were general agents of the Underwriters' Association for New Orleans and all the surrounding country. The Supreme Court said that this would have to be proved by George. Second, granting that Angomar & Co. were such general agents, George would have to prove also that they had special authority to delegate their powers to a sub-agent. Third, granting that they were specially authorized to appoint sub-agents, George should prove the actual execution of the paper which on its face purported to be a power of attorney from Angomar & Co. to Barry.

Agents, when properly authorized, *represent their principals not only in the making of contracts, but also in a thousand other matters* affecting contracts after they have been made. Some agents are authorized to receive money due under contracts, others to bring suit in the event of a breach, and still

others, called general agents, are given power to transact all manner of business for their principals. Suppose you are put in charge of a logging camp by your principal, who is a lumberman. If the land where you are working were sold, and it became legally necessary to serve a quit-notice on your employer, the notice could be served upon you as his representative in charge.

4. In addition to contractual obligations which may be fastened upon a principal through the acts of his agents, he is also responsible for *torts* committed by them in the course of their employment. We saw about torts in the fourth chapter when treating of the capacity of minors. Thousands of suits are brought against employers every year for the alleged *negligence* of their agents, and this kind of tort costs them far more than all the others combined. An employer is not responsible for torts committed by his employees quite out of the line of their service. For instance, if a wagon driver, after the day's work is over, stables his team, and afterwards uses it to take his own friends out for an evening ride, his employer is not responsible in case the driver during the evening negligently runs over somebody on the street.

A principal is hardly ever *liable in criminal proceedings* for crimes of the agent, unless he directed the agent to commit them, or took some other part in them. While an employer may be responsible for his agent's torts, although committed in direct disobedience to his orders, he is seldom liable for crimes committed by the agent, without his own participation. Personal guilt is an essential feature of most crimes.

If the agent negligently injures the person or property of a third party in the course of his employment, his principal is responsible, although the third party was ignorant at the time of the principal's existence. Likewise, where an agent makes a contract in his own name, but really for an *undisclosed principal*, the latter is liable to the third party. He was to get the benefit of the contract, and should be made to bear the burden of it. Compare this subdivision of the twentieth chapter with what is said in the thirty-seventh chapter about a bailor's responsibility to third parties for acts of the bailee.

(E) *The obligations of third parties towards the principal.*

It goes without saying that the third party is liable to the principal on contracts made between him and the principal's agent. Even if the agent had no authority when the contract was made, the contract binds the third party if the principal subsequently ratifies it. It was stated in the last paragraph that an undisclosed principal is liable to a third party. Reciprocally *the third party is liable to the principal, although he did not know of the principal's existence when the contract was made.* Where, however, the third party thinks that he is dealing only with the agent, not knowing that the agent is merely a representative, he may object to the introduction of the principal if he can base his objection on any of the rules about assignments of contracts laid down in the ninth chapter. For instance, if the third party bargained when making the contract for the personal services of the agent, the latter cannot substitute those of his principal. Again if the third party agreed in the contract to buy a certain article, from the agent, intending to set off against the price of the article a debt due by the agent, the latter could not bring his principal into the contract in such a way as to force the third party to pay the entire price to the principal, and thus to deprive him of his right of set-off.

Suppose that a salesman brings goods to your store, and you buy them, presuming him to be the owner. You pay him half the purchase money, and then receive a notice from the man who really owned them that he has discharged his salesman since the time you bought the goods, and that you are to pay him personally. If you afterwards pay the balance of the purchase money to the agent, you would be liable to pay it over again to his principal. You are protected, however, as regards your previous payments, because a man who entrusts a salesman with the possession of goods is usually presumed to give him authority not only to sell, but also to collect the purchase price. Furthermore, if the principal had known that the agent was dealing with third parties under the pretense of being the owner of the goods, he would be precluded from disputing the agent's action on the ground of estoppel, as explained in the eighteenth chapter.

(F) *The obligations of third parties towards the agent.*

The third party is usually under no duty to the agent, for the principal is the one with whom the contractual tie connects the third party. The agent has been merely the means by which the principal dealt with the third party. If the agent makes a contract with the third party, without disclosing his agency, he is personally responsible for the fulfilment of that contract. Although, in most such cases, he may substitute his principal, he remains liable himself for the fulfilment of the agreement. It would seem, however, that the agent seldom has a right to bring suit in his own name against a third party. An exception to this rule is found in the case of leases, for the agent who signs a contract for leasing property on behalf of an undisclosed principal, may bring suit on the contract in his own name against the tenant.

The third party should, when dealing with an agent, be careful to make sure of the principal's identity. It is hardly satisfactory to do business with a person who styles himself an agent, without disclosing the identity of his principal. This is particularly true of leases signed by an agent of the landlord, who fails to disclose his principal, but yet inserts a clause in the lease exempting himself, the agent, from any personal responsibility. See the case of *Holt v. Martin* (1866), 51 Pa. 499. Something more will be said about such leases in the third book.

PART II

PARTNERSHIPS

CHAPTER XXI.

FORMATION OF PARTNERSHIPS.

The study of Partnership Law branches out naturally from what we have seen about Contracts and Agency. All genuine partnerships are formed by a contract, and constitute after being formed a continuing relation among the partners. The gist of this relation is the fact that each member of the firm is at the same time a principal and an agent. He is one of the proprietors of the firm, and also becomes its agent by virtue of being admitted to membership in it. As a partnership is formed by a contract, it varies in accordance with the terms upon which the members of any particular firm may agree. This flexibility renders it difficult to draw the line between partnership and other forms of association, but the following definition has been approved by the Supreme Court of Pennsylvania: "*Partnership is a relation created by contract between two or more persons to place their money, effects, labor or skill, or some or all of them in lawful commerce, and divide the profits between them.*"

In the first place, the mere fact that two or more persons own property together does not make them partners with respect to it. Partnership involves co-ownership of the firm property, but it associates the members of a firm in a closer relation than that of mere co-owners. Each partner is a representative of the firm, while in case of mere co-ownership each co-owner speaks and acts only for himself, unless he is expressly authorized to represent some fellow-owner.

Profit sharing is an excellent test for the discovery of the legal nature of an association supposed to be a partnership.

If you find that business associates have agreed to share profits between them, it usually follows that they are partners as respects the enterprise from which the profits are to be derived. The associates have embarked together in the same business, and are jointly interested in its success. You must distinguish, however, between what are really profits, and gross receipts which are often misnamed gross profits. If you rent a farm from the owner, agreeing to pay him half the gross produce instead of money rent, he does not thereby become a partner. He is not jointly interested with you in the success of your venture, for he does not share profits with you. You may, perhaps, raise an enormous crop, so that his half will net him handsome returns, but a glutted market and low prices may prevent you from making a cent in the way of net profits, after you pay your men's wages. The produce which goes to your landlord is received by him as a substitute for rent, and not by reason of any association with you in the farming business.

Again, suppose you are running a store, and employ a manager who is to receive a share of the profits instead of wages. Even though he gets a portion of your net profits, he does not thereby become your partner, for he is not a co-principal with you in the ownership of the business. He is merely your agent. In cases like the one just mentioned it is often hard to decide whether a man is a partner or not, if the parties have not come to a clear understanding. You should always try to see whether an alleged partner who receives a share of profits takes them as a co-proprietor of the business, or merely as an agent, creditor or other outsider.

The act of June 15, 1871, allows individuals, firms and corporations to give employees, instead of regular wages or in addition thereto, a conditional interest in the profits of the business, to be regulated and determined by agreement between the parties; and the employee receiving such conditional share of profits shall not thereby become liable for the debts or losses of the business, or have any voice in the management, except as may be clearly defined in the constitution or agreement under which the association is organized or operations are con-

ducted. This act is largely intended for the regulation of special partnerships or corporations organized under some Pennsylvania statute. The ordinary partnership is formed by a contract, and is not created under any particular statute. One seeking to utilize the act of 1871 should study all its terms.

Again, doubt may arise as to your relation with a business concern *if you lend money, stipulating for a share of profits*. The courts may, perhaps, hold you liable as a partner, if the concern fails, unless you come within the provisions of the act of April 6, 1870. This act allows any person or persons to loan money to any individual, firm, association or corporation doing business in Pennsylvania, upon agreement to receive a share of the profits of such business as compensation for the use of the money, instead of interest; and such agreement or the taking of profits under it will not render the lender or lenders liable as a partner in such business, to the other creditors of the said individual, firm, association or corporation, except as to the money loaned. The act provides that the loan agreement must be in writing. It does not apply to a loan made by any member of such firm, association or corporation, or to one who holds himself out as such. If the lender stipulates for the same voice in the business and the same control as an ordinary partner, he will be held liable as one.

The difficulty of determining whether or not a given business relation constitutes the associates members of a partnership is often increased by the efforts of some of the associates to make it appear that they are not partners. Membership in a firm carries with it personal responsibility for firm debts, as we shall see later, and this prompts many to disguise the partnership relation as some less dangerous form of association. The courts, therefore, will not blindly follow the literal words in which parties may couch a partnership agreement. For instance, if A and B make a contract which has all the elements of a partnership contract, but they agree that A shall not be a partner or subject to a partner's liability, the courts will disregard these two terms because they are in direct conflict with the nature of the agreement. In the case of *Merrall v. Dobbins* (1895), 169 Pa. 480, the court unmasked

a partnership contract which was masquerading as a lease. The agreement recited that Dobbins leased to Hugh F. Griffin a certain hotel with the personal property therein contained for the summer season of the year 1892. Griffin was to give his undivided attention to the hotel business, and admission to the hotel was to be open at all times to Dobbins and his representatives. Griffin was to pay Dobbins \$20,000 rent, and also 80 per cent of the net profits. Dobbins was to designate a bookkeeper, who was also to receive and pay out all cash. Dobbins was to pay Griffin \$1,000 at the expiration of the lease, or upon its prior termination, and Dobbins was given the right to terminate the lease at any time on twenty-four hours' notice. Then the following provision was inserted, in order to shield Dobbins: "It is also understood and agreed that Griffin shall have absolute control and management of said business during the continuance of this lease; and that Dobbins shall not in any wise be liable for the business done by Griffin or for any debts or obligations which he may contract." The business was a failure, and Merrall brought suit on the theory that Dobbins and Griffin had gone into partnership. The court decided that the hotel business was, under the agreement, the business of a partnership, of which Griffin and Dobbins were joint owners, and in the profits from which they were to share as co-proprietors. Under the contract, Griffin was bound to bear all the losses, as between himself and Dobbins, but this did not affect the right of a partnership creditor to hold Dobbins personally responsible. Dobbins, having stipulated for a share of profits, and having otherwise put himself in the position of a partner, could not escape a partner's responsibility as against third persons, who had not agreed to look only to Griffin for payment. While, then, there can hardly be a real partnership without an agreement for profit sharing, there may be a partnership the members of which all agree that the entire losses shall be borne, as among themselves, by some one partner.

The contract whereby two or more persons become partners must have all the five elements described in the first six chapters. We can gather from what was said in the second

chapter that the contract may be made, first, by writing, or second, by word of mouth or, third, by conduct. If two persons conduct a business together as joint proprietors, and share the profits, they have by their acts shown their intention to become partners, although they have never used the word "partnership," or come to any verbal agreement. While a written agreement is unnecessary, it is highly desirable from a practical standpoint for the reasons explained in the eleventh chapter. The writing should cover thoroughly every term of the agreement. A specimen of such a written agreement, which is often called the "firm articles," is given below. Of course, it may be varied to meet different requirements.

PARTNERSHIP ARTICLES made this first day of September, 1906, between JULES LIT and WILLIAM DAVIS, both of Pittsburgh. Lit and Davis hereby agree to form a co-partnership, which shall continue from the date of this agreement until December 31, 1907, for the manufacture and sale of leather pocketbooks. Lit has this day turned over to the said firm the sum of five thousand dollars (\$5,000) in cash, and an equal amount, five thousand dollars (\$5,000), in machinery, fixtures, tools, patterns, raw and finished stock, and outstanding book accounts, all of which are itemized, with the respective valuation of each, in the schedule hereto attached and marked "Exhibit A." The firm accepts the outstanding accounts and other assets as being worth their appraised value, and if the said accounts or other assets should prove to be of less value, the loss shall fall on the firm. Davis contributes his skill and experience, but in the event of an impairment or loss, partial or total, of the aforesaid capital of \$10,000, both Davis and Lit shall be bound to make up the said loss, share and share alike. In the event of failure of the partnership, and of its assets proving insufficient to pay partnership liabilities, both parties shall contribute equally to pay the said liabilities. The parties shall share profits equally. Upon the termination of the firm, no matter at what time it may take place, Lit shall be entitled to receive back his contribution of \$10,000, before any profits shall be divided. If the capital shall have

shrunk to less than \$10,000, both parties shall be bound to contribute equally to make it up to the said amount, even though the excess of liabilities over assets shows a deficit, so that Lit may withdraw upon the dissolution of this firm with his capital of \$10,000 intact.

Davis shall devote his entire time and attention to the business, and shall not financially interest himself during the continuance of this firm directly or indirectly in any other business, whether conducted by an individual, firm or corporation, which deals in the manufacture or sale of pocketbooks. Lit shall devote such time as he may see fit to give to the conduct of the firm's business. In any event, Davis and Lit shall each be allowed to withdraw the sum of \$20 at the end of every week, without any right to anticipate these wages. Neither shall withdraw firm assets save as herein provided. The said weekly sums shall be considered as earned by the parties, and not as anticipated profits. Either party may permit any weekly payment due him to remain in the funds of the firm, and may withdraw same at any later period, but the same shall not bear interest. During the continuance of this partnership neither party shall make or indorse any check, note, draft or other written instrument as an accommodation for anybody, nor shall either party become bail, guarantor or surety for anybody, save with the written consent of the other party. The firm name shall be Davis & Co., and it shall do business at 125 Penn Avenue, Pittsburgh, and at such other places as may be agreed upon from time to time. All moneys belonging to the firm, and all checks, notes, drafts, and orders for the payment of money shall be deposited in the Diamond National Bank, in the firm name. Cash, not exceeding \$50 in amount, may be allowed to remain in the firm's place of business for the payment of small bills and for making change. All bills for over \$5 must be paid by the firm's checks. Checks shall be signed by Davis, but must be countersigned by Lit, except when Lit may for limited periods discontinue this requirement. Stock shall be taken, and net profits distributed during the last week of December and the last week of June in every year while this partnership continues. If the capital

of \$10,000 is found to be impaired, no profits shall be distributed until it again reaches the required amount of \$10,000. Neither party shall be liable to contribute towards increasing the capital to the fixed amount of \$10,000, save at the final dissolution of the firm, whenever that may occur. If it is found at any half yearly settlement that the capital is impaired, Lit shall have the option of terminating the partnership immediately, and if he desires to terminate it, he may act as the sole liquidating partner, and take entire charge of winding up the affairs of the firm. For his services as liquidator he shall be allowed a salary at the rate of \$15 per week for a period not to exceed two months. Davis shall keep all the transactions of the firm fully and promptly entered in suitable books of account, to which Lit shall have free access at all times. If during the continuance or liquidation of the firm, any dispute arises between the parties as to the firm's affairs, which they cannot settle between themselves, each of them shall appoint an arbitrator, and the two arbitrators thus chosen shall appoint a third. The decision of the arbitrators, or of a majority, shall be final and binding on the parties, subject to an appeal to the courts as to any legal questions involved. After the expiration of the term hereby limited for the continuance of this partnership, it shall continue for a further period of one year unless either party shall on or before November 1, 1907, notify the other in writing that he intends to terminate it; and so on from year to year, subject to dissolution at the end of any calendar year by two months' written notice. Each of the parties hereto acknowledges the receipt of a duplicate copy of this agreement.

IN WITNESS WHEREOF both parties have hereunto set their hands and seals the day and date aforesaid.

[Signed] JULES LIT (SEAL).

[Signed] WILLIAM DAVIS (SEAL).

Witnesses at signing:

[Signed] MICHAEL BURK.

[Signed] ARTHUR HORN.

If a prospective partner backs out after definitely contracting to enter a firm, he may be held liable for damages. It was held in *Creamery Co. v. Hillis* (1897), 3 Super. 527, that the injured parties may sue him for the contribution which he has agreed to make. See also *Meason v. Kaine* (1870), 63 Pa. 335, from which it appears that the relation between members of a firm is so close and confidential that the courts would only promote friction if they tried to force a man by *injunction* to become a partner. The capacity of various parties to enter into a partnership contract, and validly become members of a firm need not be treated here at length. The subject is covered by the fourth chapter, which deals with contractual capacity. Remembering that a partner is at the same time a principal and also an agent of the firm, let us apply this to what we saw in the fourth chapter about a minor's contractual capacity, and also to what we saw at the beginning of the eighteenth chapter about the validity of contracts made through a youthful agent. The contract by which a minor enters the firm is voidable at his pleasure during his minority, and for a reasonable time after he comes of age. The members of the firm who were of full age cannot in any event, however, repudiate the contracts which he made on behalf of the firm while he continued to act as a member of it. In other words, the contract whereby he became a principal may be disaffirmed by him, but the contracts which he made as agent of the partnership are binding on the other members, even if he afterwards repudiates his connection with the firm, and avoids personal responsibility.

A corporation has no contractual capacity to go into a partnership. Corporations are associations regulated by statute law, which designates a certain method by which the associates shall be represented. The corporate directors and officers are the persons in whom this representative authority is lodged, and it would be altogether beyond the powers of a corporation to put any such authority in outsiders, as partners of the corporation itself, instead of in those to whom it rightly belongs.

It was noted in the eighth chapter that besides various kinds of genuine agency, as spurious agency is sometimes

created by estoppel. It is not real as between the principal and the agent, but it may have the same consequences as real agency, so far as innocent third parties are concerned. This idea applies equally to cases of partnership. If the members of a partnership hold you out to the world as being a member, although you really are not, and you impose on innocent third parties, assuming to act as one of the firm, the firm is liable for acts done by you in its name, and within the scope of your apparent authority as a partner. This shows that the doctrine of estoppel may make your acts binding on the firm, if the real members have clothed you with the appearance of being one of their number. Now reverse the situation, and see how the doctrine of estoppel may affect you with the same liability as a principal, if you hold yourself out as a member, or permit others to hold you out as one. Suppose your name is Black, and you are employed by persons of the same name who are in partnership under the name of Black & Co. This of itself would not subject you to the liability of a partner, but if you are often spoken to on the supposition that you are in the firm, and do not correct the mistake, a third party who is misled thereby could hold you liable as a partner, in case the firm failed. You would preclude yourself from proving that you are really not one by your silence under circumstances which make it your duty to speak out the truth. We should clearly distinguish between those who are actually partners and those who are only partners by estoppel. The latter have none of the rights of partners, and they are considered such only when the courts desire to adopt this fiction in order to prevent injustice towards innocent third parties. Suppose a firm composed of A and B fails, owing money to two creditors. C has represented himself as a member of the firm to one creditor, who gave it credit in the belief that C was in it. This creditor may hold C liable as a partner by estoppel. If the other creditor had no idea that C was in the firm, C will not be liable to him. Now suppose that A and B knew of C's misrepresentations, and suppose the firm made a big success. C could not claim a share of profits on the basis of being a partner, for he is not really one.

A case which shows that those who are partners by estoppel towards outsiders do not thereby become partners in reality, is that of *Fitzsimmons v. Robb* (1899), 193 Pa. 518. The parties to this suit had for many years occupied the same office building, for the practice of law, and the name "Robb & Fitzsimmons" was displayed on this building, and also printed on letter-heads used by both parties. The same joint name was used in suits brought in the various courts. In 1895 Fitzsimmons brought suit by filing in court a "bill in equity," in which he alleged that Robb had been his partner, and petitioned for an accounting between himself and Robb, and a division of the fees earned during the period of their association. He proved that Robb had often referred to him as a partner. From these facts it was clear that a third person would be justified in believing that the two were in partnership, and in holding Robb jointly responsible with Fitzsimmons for whatever the latter might do on behalf of the alleged firm, and within the scope of the business of a law partnership. The court in this case had to consider, however, not how the association appeared towards outsiders, but what it really was as between the parties themselves. Robb proved that during the entire period of his connection with Fitzsimmons he had attended to criminal business, while Fitzsimmons took charge of civil business. Each had received and retained the fees earned in his own line. Both had been concerned together in a few special cases, which had been settled, and the fees had been divided as received. No partnership books had been kept, and no settlement on the basis of a partnership had ever been made. The first suggestion by Fitzsimmons of indebtedness from one to the other was made after he had been associated with Robb for fifteen years, and no demand had been made by him until the day when the two severed relations. The court decided that there had been no general partnership between Robb and Fitzsimmons. They had, perhaps, been law partners within a narrow range which was confined to the few cases handled by them jointly. These cases, however, had all been disposed of long before Fitzsimmons brought suit, and the slender partnership relation which had existed as to such cases had been previously dissolved.

CHAPTER XXII.

THE TERMINATION OF PARTNERSHIPS.

In considering how partnerships are brought to an end, we may refer to the chapters on the discharge of contracts and to the chapter on the termination of agency. Following the subdivisions which were made in those chapters, we shall study the termination of partnerships as caused, first, by agreement; second, by performance; third, by breach; fourth, by impossibility; fifth, by bankruptcy.

(A) Termination of partnerships by agreement.

The members of a firm are free to dissolve it at any time, although it was originally meant to run on for a longer period, provided they all agree to the dissolution. If no time has been fixed for the termination of the firm, it may easily be dissolved by any member's notifying the other members of his intention to withdraw. A partnership consists of a certain group of individuals, and the retirement of a single member necessarily changes the group and thereby dissolves the firm. A new member may be substituted for the old one, but the group is no longer the same. Although the firm name may continue unchanged, the substitution of the newcomer results in the formation of an entirely distinct firm. The accounts of the new concern should be kept with this fact in mind, and the various rights and liabilities of the partners should be adjusted accordingly. If a firm composed of A, B and C is dissolved on January 1, 1906, by A's retirement, and a new firm, composed of B, C and D, is at once started, A's net interest in the old firm should be computed as of the date of his withdrawal, unless there is an agreement to the contrary. He remains liable to outsiders on contracts made before his retirement, but is not responsible for subsequent contracts. D is not liable to outsiders on firm contracts made before he became a member of the firm, for his liability commenced as of January 1, 1906.

D was not a party to the previous contracts. The continued use of the same firm name despite changes in membership is often confusing, for one should remember that the firm name is only a convenient handle by which to designate a certain partnership group. You should look behind the firm name and see who are the individuals composing the partnership at a given time, for these individuals are parties to any contract which their firm may make. Bearing in mind the statement in the eighth chapter that usually nobody save the immediate parties to a contract is interested in it, you can apply this to such partnership transactions. You should remember also what was said in the ninth chapter about the assignment of contracts, for a new partner may sometimes be substituted for an old one. We shall see later that the other members must consent to the introduction of the new partner, and in any event the change of membership results in the termination of the old firm and the creation of a new one.

While the retirement of a partner usually prevents him from being liable on subsequent firm contracts, he may sustain this liability upon the doctrine of estoppel. In the preceding chapter we saw that an outsider may be held to partnership liability if he helps to mislead innocent third persons into trusting a firm in the belief that he is a member of it. The outsider who runs the greatest risk of being made responsible as a partner by estoppel is one who was formerly in a firm, and withdrew without giving notice of his retirement. If you are in business with John Smith, under the firm name of John Smith & Co., and you retire, you should notify all those who have had dealings with the firm. The notice should be mailed by registered letter or served personally by a messenger who should, if possible, get every party upon whom he serves notice to sign a receipt acknowledging the delivery of it. Another way is to print the notice on a postal card with an attached return postal. Upon the return postal you can have printed a form of receipt which the recipient of the notice may sign. Furthermore, you should advertise the fact of your retirement in at least one local paper.

In most cases, perhaps, no harm will result from a dis-

regard of these precautions. The disregard may cause you trouble, however, if your late partner continues in business under the same firm name, and afterwards fails, for you may be held responsible upon subsequent contracts by those who were unaware of your withdrawal. The following is a typical form of notice of change of membership in a firm, which may be varied to suit different cases:

PARTNERSHIP DISSOLUTION.

READING, June 1, 1906.

The firm of Myers & Langbein is dissolved this day by the retirement of Mr. Gustave Myers.

GUSTAVE MYERS,
ADOLPH MYERS,
FRITZ LANGBEIN.

The business will be continued at the same place and under the same firm name by the following:

ADOLPH MYERS,
FRITZ LANGBEIN,
ANTON SNYDER.

After a firm has been dissolved, the members cease to have authority to bind each other, except in so far as may be necessary to wind up its business. See the case of *McCahan v. Smith* (1899), 9 Super. 318. Any one of the former partners has authority to receive money due the firm, and to give a valid receipt. See section 77 and section 99 of the negotiable instruments act in chapter ten, relative to serving certain notices upon members of a dissolved firm. Usually the members choose one or more of their number to liquidate affairs. Only a liquidating partner has any authority to bind his former partners by new contracts. Even the liquidating partner's powers in this respect are limited. He cannot confess judgment against the others without their consent. He may, however, sign a renewal of a firm note. He may also sign a note with the firm name in settlement of an account with any

of its creditors. He may acknowledge the existence of a debt on behalf of the firm with the effect of preventing the debt from being outlawed.

(B) *Termination of partnerships by performance.*

A partnership agreement may provide that the firm shall last for a fixed period, and if notice is not given within the period that it shall continue, say, another year. Assuming, however, that a firm is formed for a certain period and nothing is agreed upon as to its continuance thereafter, it will come to an end at the expiration of the time named. The agreement of partnership is performed at the completion of the period. Notice need not be given beforehand by any partner. The firm comes to an end when the span of life agreed upon for it has elapsed. Of course, the parties are free to continue together by a subsequent agreement, which may be made in writing, or by word of mouth, or by conduct.

Again, if the partnership has been formed without mention of the time during which it is to last, it will be terminated upon the final performance of the undertaking for which it was created. If A and B become partners merely to carry out a certain tunnel contract, the completion of the tunnel and settlement of the accounts concerning it mark the firm's dissolution, without any notice by either partner.

(C) *Termination of partnerships by breach.*

We shall see in the following chapter that the intimate relation between partners requires them to display the utmost good faith towards each other. A violation of this duty may justify the injured party in seeking a decree of court to dissolve the firm. Suppose that A and B are in partnership, and that the firm articles impose on B the duty of keeping proper books of account. If B fails to keep the books with any care, and refuses to let A see them, A may obtain a decree of dissolution. Again, if one partner misapplies funds of the firm towards the payment of his private debts, to such an

extent as to impair the capital which the partners have agreed to keep in the firm, the other members who did not consent to this action may have the concern dissolved. It would seem that small payments out of firm funds, duly entered in the firm books, to liquidate one partner's private debts will not enable the others to obtain a dissolution, if the solvency of the firm is not endangered, and if the partner has not broken any specific agreement. Hence the advisability of inserting in the firm articles a strict provision about the withdrawal of funds. The courts are opposed to decreeing the dissolution of a firm before the time fixed by the partnership articles merely for slight acts of negligence or blunders which do not savor of fraud, where the existence of the firm is not imperiled, and where all the matters complained of can be fully adjusted in the final accounting. Mere errors of judgment constitute no ground for dissolution, unless they are likely to ruin the firm.

When a member ceases to take any part in the firm business, against the wishes of the others, the latter may have the firm dissolved. The partnership consists essentially of certain individual members, and if one of them abandons the group, the others may have the firm wound up. This happens if a partner sells his interest to a stranger, or even to one or more of his fellow partners, unless otherwise provided by agreement. If A, B and C form a partnership, and B sells his interest later to C, it is only proper that A should have the right to terminate relations with C at once, although the firm may have been intended to last for a longer period, because A may regard B's membership as necessary to its success.

(D) Termination of partnerships by impossibility.

This fourth method of discharging the partnership contract operates mostly in the case of the death or permanent incapacity of one of the partners. The executor or administrator of the deceased member need not notify those who have dealt with the firm that it has been dissolved. They are supposed to learn for themselves about the member's death. Likewise, if a member is adjudicated insane in a lunacy proceeding, the

decree of court finding him insane is deemed legal notice to all the world.

In order to avoid the awkward consequences of one partner's sudden death, some firm articles provide that the share of any member who may die shall be allowed to remain in the firm for, say, one year, and that the surviving partners need take no steps to wind up the concern until the expiration of the said year. In the absence of an agreement to the contrary, the executor or administrator of the dead man has usually no voice in the management of the firm affairs. He should not schedule the firm assets in the inventory of the decedent's effects, for usually the decedent's estate is entitled to nothing but the sum which may ultimately be found due the decedent upon the complete liquidation of the firm's affairs. Sometimes the firm articles provide for the purchase by the surviving partners of a deceased member's interest at a price either fixed by the articles or to be determined afterwards by appraisers. This saves the expense and delay of accounting. If a partner provides by will that his interest shall remain in the firm, and the surviving partners consent, pretty much the same result is accomplished as if there had been an agreement to that effect during the lifetime of the decedent. There is this difference, however, that the decedent's creditors have a right to object to any provision of the will which postpones the payment of their claims beyond a year. On the other hand, if there is a contract made by the partners before the decedent's death, the creditors cannot object to its being enforced, unless they can show either that it was intended to defraud them or that it will tie the estate up for such an unreasonably long period, say twenty years, as to justify the court in setting it aside.

We shall see in the following chapter what each partner is entitled to out of the firm estate upon its dissolution. Of course, when the firm is dissolved by death, the executor or administrator of the partner who has died is ordinarily allowed to receive exactly the same amount as would have been received by the deceased partner himself, were he still alive. The surviving partner is bound to wind up the affairs of the firm,

and can charge no compensation for his work in this direction, unless the firm agreement provides otherwise. On the other hand, the surviving partner cannot usually be charged with the value of the good will in case he continues in the same business. *Musselman's Appeal* (1869), 62 Pa. 81. Likewise, if a partner owns the property where the firm conducts its business he is entitled, upon dissolution, to the good will of the business so far as it is incidental to the property. *Rafferty's Estate* (1886), 18 Phila. 14. See also *Johnson's Appeal* (1886), 115 Pa. 129. Some firm articles contain a provision that the surviving partners shall pay a certain sum to the estate of any deceased partner for his interest in the good will. If, however, your good will is a valuable asset, you can ordinarily make it worth more to your estate by incorporating your business.

(E) *Termination of partnerships by bankruptcy or insolvency.*

The mere fact that the partnership is insolvent does not of itself cause a dissolution. It may be that by struggling along the firm will be able to pay its debts, and continue business successfully. Usually, however, one of the partners may obtain a decree from the court dissolving the firm, on the ground of insolvency. If an assignment of all the firm's property for the benefit of creditors is made, and there is no provision for continuance of the business, the assignment coupled with the stoppage of business brings about a dissolution. Of course, if the firm goes into bankruptcy, under the provisions of the act of 1898, it is dissolved. Section five of this act, which will be found in the seventeenth chapter, relates to bankrupt partnerships.

Going into bankruptcy under the provisions of the act of 1898 has more serious consequences than simple insolvency. The insolvency of a partner does not necessarily dissolve the firm. It may have that effect if a creditor of the insolvent member gets judgment against him, and has the sheriff sell out his interest in the firm. This involuntary transfer of his interest has the same effect in dissolving the partnership as

if he had assigned his interest voluntarily. If a partner goes into bankruptcy, his interest in the firm passes by operation of law to the trustee appointed by his creditors, and this causes a dissolution of the firm, unless the firm articles clearly provide otherwise.

CHAPTER XXIII.

RIGHTS AND OBLIGATIONS OF PARTNERS.

The rights and obligations of a partner may be considered in two lights: first, as respects his fellow-partners; second, as respects outsiders. It will be helpful to remember what was said in the twentieth chapter about the rights and obligations arising under the agency relation, and the reader should compare the rules of partnership law with those governing agency. As a partner is both a principal and an agent, we shall consider his relation towards his fellow-partners: first, as respects his proprietorship; and, second, as respects his power to represent the firm.

(A) The relation of a partner towards his fellows as a co-proprietor of the firm.

While a partner is one of the co-owners of the firm's assets, it by no means follows that he can sell for his own exclusive benefit a proportionate part of each piece of property belonging to the firm. Suppose A and B are equal partners, and the firm owns a trade-mark. Strictly speaking, A does not own a one-half interest in that trade-mark, but rather a half interest in the firm, which in turn owns the trade-mark. If A were to die and leave his estate to his wife, the wife would not become a co-owner of the trade-mark with B. The partnership property is a separate fund, and must be kept by itself for the benefit of the firm business, and also to preserve the rights of A's co-partner, B, and of firm creditors. In the first place, the trade-mark may be needed in connection with the disposition of the other firm assets. Perhaps B, as liqui-

dating partner cannot sell the rest of the firm property to advantage unless he can sell along with it the full ownership of the trade-mark. In the second place, it may be that A has overdrawn his account with the firm, or that B, his partner, has loaned money to the firm. After adjusting these matters, it may be found that A's share in the firm is not worth a cent. In the third place, it may be that the firm owes creditors more than the total value of its assets, so that A's share in the firm is a minus quantity; that is, A's estate should put up money to help meet firm liabilities, rather than take anything away from the firm's assets.

A partner's interest in the firm, therefore, is only that share which may be found due him upon settlement of the accounts. Accordingly, if he sells his interest to a stranger, the latter does not buy an absolute right of property in the firm assets, but only a right to receive whatever may belong to the partner who sells out after paying off firm creditors and dividing the balance in accordance with the respective rights of the members. Therefore, if you are in partnership with B, and B's creditors get judgment against him, they have no right to sell out the firm property. They may send the sheriff to dispose of B's interest in the firm. The purchaser who acquires this interest would ordinarily have a right to demand an accounting from you. The accounting might, perhaps, show that B had, before the sheriff's sale, drawn out the money contributed by him, and borrowed so much other money from the firm that his interest in it would be less than nothing. Of course, in that case the purchaser could not require you to pay him anything, but if, on the other hand, B's interest were found to be worth \$1,000, the purchaser would be entitled to that sum out of the firm's assets.

A partner has no right to thrust an outsider into the firm, and make him a member of it, save with the consent of all his co-partners. If the members have not agreed to remain in the firm during a certain period, one of them may at any time assign *his interest* in the firm to a stranger, but *he may not assign his right to be a partner.* In other words, he may transfer his mere co-ownership and so give his assignee the same

right to an accounting that he had himself, but he may not transfer his right of control over firm affairs or his right to represent the firm in transactions with third parties. *The property interest which he enjoys as principal is assignable, but not the representative authority which he possesses as agent.*

(B) *A partner's authority as an agent of the firm.*

The amount of authority possessed by partners varies not only with the nature of the partnership business, but also with the terms of the firm articles, where the members have specially provided for this matter. Generally speaking, however, we may say that any partner, acting by himself, has authority to bind the firm in all matters within the real or apparent scope of its business. Each partner is, therefore, a general agent of the firm group to represent it within the limits of the joint enterprise. This results from the nature of his relation with his fellow-partners. Even though the firm articles restrict the powers of a certain partner, his actions on behalf of the firm will bind it, unless the third parties with whom he deals know that he is overstepping his real authority. His position as partner gives him the outward semblance of authority to act on behalf of the firm, and the doctrine of estoppel prevents the firm from repudiating what he does within the apparent scope of his powers.

The authority of a partner, as implied from his being a partner, must be measured by the nature of the firm's business. A broad distinction should be drawn between *professional partnerships* and *strictly business partnerships*. In the latter class are included mercantile, manufacturing, mining, and other partnerships which naturally involve the use of firm property and firm credit. These are different from professional partnerships, for in the latter the idea of firm capital is rarely present. In a law partnership, for instance, the members associate to gain the advantages of co-operation, but the firm property is of comparatively slight importance. One member of a law firm may probably bind the partnership group by a contract

for the purchase of lawbooks or office furniture, but his implied powers do not extend so far as to enable him to borrow money in the name of the firm. Of course, if the other members of the firm ratified such a loan, the firm would be liable.

In the case of strictly business partnerships, each member has implied authority to borrow money on the credit of the firm. The firm group is liable, even though the member who borrowed the money was expressly forbidden to do so, and even though he put the money in his own pocket, unless the lender knew that he was abusing his trust. The lender should be on his guard if the amount asked for is out of proportion to the firm's apparent needs, for if he has good reason to suspect that the partner is overstepping bounds, he cannot hold the firm liable. Thus if a partner gives a note signed with the firm name in payment of a private debt due by himself, his creditor should take notice that the transaction looks suspicious, and cannot hold the firm group unless it really authorized the making of the note. Nevertheless, if the note is negotiable, and is indorsed to an innocent holder for value, the latter may recover against the firm, in accordance with the rules stated in the tenth chapter. Besides the implied power to borrow money and to sign negotiable paper in the firm's name, each member of a strictly business partnership has *authority to buy on the firm's credit* such goods as are apparently suitable to its business. If the firm is in the business of selling goods, each partner has a similar implied authority to make sales on its behalf. He has no authority to make sales out of the ordinary course of business. For instance, a single member of a firm which runs a large department store has no implied authority to dispose in bulk of all the stocks of merchandise in the various departments, for this would be out of the regular course of business. It would be an act, not in the ordinary running of the business, but rather in the direction of winding it up entirely. In such a sweeping measure all the partners should join.

One partner has usually *no implied authority to sell partnership real estate*. Of course, if the title to firm realty has been put in the name of only one partner, without any apparent

restriction on his authority, his deed will convey a good title to an innocent purchaser, even though he has violated a private agreement on the subject. The proper way to hold firm real estate is to have the title conveyed to all the members, not as individuals, but as members of a firm. Thus, if A, B and C, who compose the firm of A & Co., want to buy land for their firm, the title should be conveyed to "A, B and C, trading as A & Co." The mention of the firm in the deed is record notice to all the world that none of the partners has an individual right to the realty, but only such an interest in it as may be found due him upon payment of firm creditors, and adjustment of the partners' respective rights and obligations. Any single member of a partnership formed to deal in realty has, perhaps, implied authority to buy or sell realty for the firm.

A partner has *no implied authority to confess judgment against the firm*, for this is a very serious matter, and is outside the limits of ordinary business. Usually the confession of judgment is brought about by the signing of a judgment note, which authorizes the entry of judgment in court against the party who makes the note. It seems also that a partner has *no implied authority to bind the firm by an instrument under seal*, although, of course, the partner who exceeds his authority in executing such an instrument is personally liable on it. Again, a partner has no implied power to make a contract of *guaranty or suretyship* on behalf of the firm, unless such a contract is in the regular line of its business. Any single member of a firm of note brokers probably has implied authority to make special contracts guaranteeing the notes of third parties in various respects.

As a partner is naturally a general agent of the firm, his power to act for it extends not only to the making of contracts, but also to hundreds of other things in the course of firm transactions. He may be served with legal notices intended for the firm. A suit against the firm may be commenced by serving a single member with the writ. It is better, however, where you fear that the firm may fail, to have the writ served on each individual partner. If only one is served, and you obtain judgment in the suit thus commenced, the judgment will

bind the firm, for the partner served was its agent for such purposes. *He was not the agent, however, of the other individuals* composing the firm. If the firm fails and its assets are insufficient to pay the judgment, the creditor may proceed against the private property of the partner served, whom the judgment binds personally. If this partner's private property is insufficient for the purpose, the creditor cannot send the sheriff to sell the separate property of the other partners until he has served them personally with his legal writs, and gone through the stages of a lawsuit with them.

In a suit brought by or against a firm, it is improper to use merely the firm name. The individuals composing the group should all be named. Thus, if Thomas Farr and Eva Ward do business under the firm name of "Farr's Novelty Store," you should not bring suit merely against "Farr's Novelty Store." You should sue them as "Thomas Farr and Eva Ward, trading as Farr's Novelty Store." Sometimes it is hard to discover who are in a firm against which you wish to bring suit. Perhaps the information may be obtained in the prothonotary's office of the county where the firm does business. The act of April 14, 1851, provides that all persons doing business in a partnership capacity in Pennsylvania shall file, in the prothonotary's office of the county or counties where the partnership is carried on, the names and locations of the members of such partnership, with the firm name; and as often as any change of members in said partnership shall take place, the same shall be certified in the prothonotary's office by the members of such new partnership; and in default or neglect of compliance with this act, they shall not be permitted in any suit or actions against them, to plead any misnomer or the omission of the name of any member of the partnership, or the inclusion of names of persons not members of said partnership.

It often saves trouble for business houses to learn the names of those who compose a firm when they first begin to have transactions with it, and to enter the names in their ledgers. For instance, instead of opening an account with "Farr's Novelty Store," mentioned in the preceding paragraph, a bookkeeper should open it with "Thomas Farr and Eva

Ward, trading as Farr's Novelty Store." When a check is received from a debtor many careful bookkeepers make a memorandum on their ledgers of the bank where the debtor keeps his deposit. This information may be useful in a lawsuit.

Returning to the subject of the partner's relation to the firm as its agent, we should note that he owes it the highest loyalty. He is even closer to the other members of the group than the ordinary general agent, and this confidential association imposes a 'corresponding duty on him. What was said in the twentieth chapter about an agent's obligation towards his principal applies here. The case of *Bast's Appeal* (1872), 70 Pa. 301, shows that a partner should not try to profit selfishly in transactions which are in line with the firm's business. Davis Pearson was in a coal firm with Emanuel Bast, Robert Taylor and R. M. Lindsey. A man named Tucker came to the firm's office and informed Pearson of a chance to make a profitable contract. Pearson arranged to have a clerk in the office make a proposal in his own name, with Pearson as his surety. The contract was awarded to the clerk, who assigned it to a syndicate, composed of Pearson and five coal companies. Pearson got his firm to furnish some coal to the syndicate, and the firm made a profit on this end of the business. Pearson's share of the syndicate's profit was over \$27,000, half of which he paid to Tucker as a gift. The other three partners sued for a share of the profits realized by Pearson, measured by their respective interests in the firm. They were allowed to recover, because it is an implied duty, without any stipulation on the subject, that every partner shall abstain from any business which will necessarily deprive the firm of a portion of the skill, industry, diligence or capital which he is bound to employ therein. Of course, any partner may be released from this duty by the agreement of his fellows. In the absence, however, of such an agreement, each partner is in a fiduciary relation to the others, and must devote all his energy to the advancement of the firm exclusively, and account for all moneys received by him through its legitimate business.

Bast's appeal is a strong vindication of the foregoing

principles, because Pearson's partners took no action for three years to compel a division with them of the profits received from the syndicate, and did not bring suit until after his death. The court excused this, because Pearson had remained in the firm up to the time of his death, and no final settlement had ever taken place. It was not unreasonable to suppose that the three other members of the firm, who were younger than Pearson, had awaited a period of final settlement, in confidence that the matter would be fully accounted for then. Furthermore, in compelling Pearson's executors to pay over a large portion of the syndicate's profits, the court refused to give them credit for the half portion of such profits given by Pearson to Tucker. Since Pearson chose to give this voluntarily, he was not released from accountability for it. His generosity to Tucker was at his own expense. He was a trustee for the firm, and could not legally apply its funds to anything but the firm business without the consent of his partners. The gift of half Pearson's portion of the syndicate profits was not made in the line of firm business, since Tucker had no contractual right to share in them.

Compare *Bast's Appeal* with *Geddes' Appeal* (1876), 80 Pa. 442. Geddes was a member of a firm, and some of his co-partners sent Thomas Beaver to buy out his interest. After selling it to Beaver, he learned that the latter was merely an agent for other members of the firm. Geddes filed a bill in equity to have the sale set aside. He asserted that it was an abuse of the confidential relation between the partners to employ a stranger to purchase his interest, and to conceal from him the fact that some of his co-partners were the real purchasers. The court decided against Geddes, for the contract for the sale of his interest in the firm was not a firm contract. It would have been fraudulent for his co-partners to have made a contract with their own firm through Beaver, without disclosing their identity. *The contract with Geddes, however, was a contract between individuals, for the sale, not of firm assets, but merely of Geddes' share as one of the firm proprietors.* His share was his personal property, in the same way that his private residence was his own. If Geddes' co-

partners had employed Beaver to negotiate for his residence, they would be under no duty of disclosing that they were back of Beaver, merely because they were in the same firm with Geddes. *A partner is a general agent, not of his co-partners as individuals, but of the firm group.* His authority relates to firm property and firm business.

Since a partner is bound, in the absence of an agreement to the contrary, to devote all his efforts towards advancing the interests of his firm, *he cannot claim any compensation for his services.* He is a principal in the firm, and is presumed to look for his reward to the profits, if any, which may be made by the concern. Accordingly, a partner who does more than his share of the work should bargain for special compensation. If he waits until the final accounting, he will find that he has no right to present a claim for what he did as agent of the firm. His position as principal raises a presumption that he is to get his pay out of the profits, if any, which he takes as a co-proprietor.

A partner should be careful not to mingle firm funds with his own. The partnership property should be kept entirely distinct from that of its members. If one partner allows the firm to use articles belonging to him, he should have a written understanding to the effect that he does not contribute them to the firm, and that they remain his private property. The danger of confusing individual and firm accounts appears from the case of *Lefever v. Underwood* (1862), 41 Pa. 505. These parties entered into a partnership for buying and selling cattle. Lefever took active charge of the purchases and sales, and banked the money in his own account. Underwood mistakenly supposed that firm funds were deposited in the firm name, "G. W. Lefever & Co." The Lancaster Bank, where the money was deposited, failed, and Lefever took its notes, payable to himself for the amount standing to his credit. Part of his notes were redeemed, and the others gradually dwindled in value until they became almost worthless. Underwood took no part in these arrangements, Lefever conducting everything. The court held that Lefever must sustain the whole loss. He had treated the account with the bank as his own individual

account, and the arrangements about the notes were made in the same spirit.

The firm is responsible for the torts of a partner committed in the course of his work as its agent. In the case of injuries received through the negligence of a partner by an employee who is working with him, the firm cannot successfully defend on the ground that the partner was a fellow-servant with the employee. The partner is a principal. Again, if a partner authorizes an agent to act on behalf of a firm, the employment is made in his capacity of principal. The other partners cannot repudiate the delegation of authority on the ground that an agent may not appoint a sub-agent without special permission to do so. The agent appointed by a partner is not a sub-agent, for he was directly employed by a principal. The power to engage agents varies with the range of the partnership business, for some firms naturally require more agents and higher priced ones than others. Every firm may need legal counsel in lawsuits, and any partner has implied authority to employ an attorney-at-law to defend the interests of the firm. If two partners employ, each a different lawyer for the firm, the latter will be liable for the compensation of both counsel.

Where a dispute arises among the members as to the way to conduct firm affairs, the majority governs. Of course, if the majority uses its power fraudulently, the minority may invoke the aid of the courts. If there are five members, and two, who own the majority interest of the firm, vote against the other three, the majority in number will prevail, unless the firm articles provide otherwise. The articles should contain a provision for the speedy and harmonious adjustment of disputes, as for instance by arbitration.

(C) A partner's obligations towards firm creditors.

As every partner is a member of the firm group, he is individually obligated to make good every firm liability. Debts of the firm should be paid out of the firm funds, if possible, but the partners are ultimately liable in case the partnership

assets are insufficient. Even a partner who has, say, only a one-twentieth interest in the firm may be compelled to pay all its debts without limit, if the firm fails. Suppose the other partners have agreed that he shall be excused from personal responsibility for partnership debts. *This cannot affect the rights of firm creditors, unless they themselves agree not to look for payment to the individual who is seeking exemption.* Of course, if a partner, whose fellows have agreed to shoulder all firm liabilities, is compelled by creditors of the firm to pay its debts, he has a right of action against his co-partners to recover part of what he pays. He may perhaps find, however, that if he gets judgment against his co-partners, it will not be collectible. *There is no convenient device whereby one may become a member of the ordinary partnership, and acquire a right to share in its profits, and to help control its affairs, without assuming an ultimate responsibility for its debts.*

Suppose a partnership fails, with assets worth \$5,000 and liabilities of \$10,000. Suppose \$7,500 is due outside creditors, and the remaining indebtedness of \$2,500 is due one of the firm. The latter would not be allowed to compete with the outsiders for a dividend from the insolvent firm's assets. Being a principal of the firm, he is personally liable for all its debts, and so is at a disadvantage as compared with the other creditors. As regards his own claim against the firm, he is not only a creditor, but to a certain extent a debtor also. The case of *Oyster v. Short* (1896), 177 Pa. 594, proves that the foregoing rule cannot be altered by the private agreement of the partners themselves. Hezekiah Horton entered into a banking partnership, which conducted business under the name of Ridgway Bank. The firm articles provided that in case any member should die, his executor or administrator would be entitled to the return of the capital advanced by the decedent, and also to his proportionate share of one dividend (to be made out of half the net surplus at the time of his death), in full settlement of all his interest in the partnership. The remaining members were to continue, fully assuming all firm debts, and becoming the owners of all firm assets, just as if the decedent had not been in any way connected with the Ridgway Bank.

Horton died in November, 1892, and seven months later the bank went into the hands of receivers. Horton's administrator demanded a dividend upon the amount of capital which Horton had put into the firm, but the court refused to allow it. The outside creditors of the bank were entitled to priority, and until they were paid in full nothing could be given by the receivers to Horton's estate. The private agreement of the partners could not abridge or change the rights of creditors who were not parties to the firm articles.

Suppose that a firm composed of four members, A, B, C and D, fails, and that two of the partners, C and D, are also individually insolvent. These two individuals are unable to pay their private indebtedness. How shall the rights of the various creditors be adjusted? The partnership funds are kept separate for the payment of firm creditors. Likewise, the private fortune of C is kept apart for C's personal creditors, and D's private fortune is reserved for his personal creditors. The firm creditors would not have a right to participate in C's funds until after C's creditors were paid in full. The firm creditors may, of course, sell out the private property of A or B, who, let us suppose, are solvent. C's private creditors would have no right to a dividend out of the firm estate until firm creditors were paid in full, and even then only to the extent of C's proportionate interest in the firm. Of course, C's personal creditors would have no claim against D's estate in any event, or against the individual property of A and B.

(D) Partnership accounts.

Much trouble would be spared the members of many firms if their accounts were carefully kept from the very formation of the partnership relation. The firm's journal or ledger or other appropriate book should show the respective share or interest of each member. All contributions to firm capital should be appraised, where not made in money, and should be promptly and completely entered on the firm's books. Loans by partners to the firm should appear as such. Where partners are allowed to draw salaries, their with-

drawals on this account should be clearly distinguished from advances on account of anticipated profits, and from sums borrowed by any partner under an agreement to repay them, as well as from any share of profits received by a partner upon the payment of dividends by the firm. The firm books should contain sufficient data to enable an auditor to prepare an accounting between the partners without consulting anything else.

The relations among the members of a firm are usually so complex that they cannot be accurately stated without an accounting. There are ordinarily many items of debit and credit to be considered before the condition of the firm can be ascertained, and hence it requires careful calculation to learn the value of the interest of any particular partner. It would produce endless confusion if members of a firm were allowed to adjust their respective rights by suits and cross-suits. Suppose X advances some money to prevent his firm from being sued for a debt. If he were to bring suit against B and C, his co-partners, to force them to pay a proportionate share of the debt which he has just cleared off, they might answer that they also had paid other debts of the firm with their personal funds. X might reply that what B and C had paid out for the firm was counterbalanced by advances to B and C from the firm's treasury. In this way the litigation would become more and more tangled, so the courts forbid partners to sue each other in such matters pertaining to firm affairs, except where the partnership has been involved in only a single transaction. The proper way to solve the difficulty is to have a full accounting of all firm matters, and a settlement in accordance with the results reached. Into this accounting should enter all matters pertaining to the firm, and to the relation of the partners with it.

We have seen that each partner is liable without limit for firm debts, in case firm assets are insufficient. Suppose a firm, composed of A and B, fails, but both partners are personally solvent. The firm creditors may choose to pursue B alone, and they have a right to compel him to make good out of his private fortune the firm debts remaining unpaid. B cannot

usually compel them to proceed against A's property, and thus satisfy half of their demands out of the personal assets of each partner. B has, however, a right to demand an accounting with A, and B may credit himself at this accounting with moneys paid by him to settle firm debts.

When a partnership is formed there should be a clear understanding as to the amount of capital which each member is to contribute, and his respective share in profits and losses. If the firm capital is always to be maintained at a certain figure, this should be stated, and the method proposed for assessing the members to make up an impairment of capital should also appear. See the specimen form of partnership articles given in chapter twenty-one.

In the absence of an agreement on the subject, all partners ordinarily share equally in the profits, and usually it is considered that the burden of meeting firm losses should be sustained by the partners according to the same proportion in which they were to benefit by the firm's success. Before profits can be computed regard must be had to the amount of capital invested by the various partners, and upon the dissolution of the firm each partner is usually entitled to withdraw the amount of capital contributed by him. If one partner has furnished all the capital, and the other has furnished skill and experience, the former will be entitled to withdraw the entire sum which he contributed.

Likewise, it would seem that if the whole firm capital, say \$10,000, is contributed by one partner, and if the firm's failure wipes this capital out of existence, the other partner cannot be called on to make good half the capital so lost. Suppose, however, that in addition to losing all its capital, the firm has to meet liabilities of \$2,000 more. Each of the partners ought to pay half this amount. The capitalist, therefore, would be out of pocket a total of \$11,000, while his partner would be out only \$1,000. These principles are subject to variation through special agreements which firm members may make with each other. See the following cases: *Everly v. Durborrow* (1871), 8 Phila. 93; *Emerick v. Moir* (1889), 124 Pa. 498; *Yohe v. Barnet* (1841), 3 W. & S. 81; *Brenner*

v. Carter (1902), 203 Pa. 75; *Brenner v. Carter* (1900), 9 D. R. 511.

Singizer's Appeal (1857), 28 Pa. 524, furnishes an illustration of the practical application of the simple principles of partnership accounting. George Keeseman had been in partnership with Singizer, who died. Singizer's administrator collected \$295 due the firm, and paid off firm debts amounting to \$995. Keeseman also collected money due the firm, applying all that he received towards its debts. Later he assigned his individual property for the benefit of his creditors. Singizer's administrator demanded a dividend out of Keeseman's assigned estate, asserting that Keeseman was indebted to Singizer in the sum of \$350. His calculation was made by subtracting \$295 from \$995, and dividing the balance, \$700, into two parts. \$350, one-half of \$700, he contended, should be paid by Singizer's estate, and the balance constituted an obligation of Keeseman. The court refused to allow the administrator to get a dividend out of Keeseman's estate, for no settlement had ever been made between the partners. Until a partnership accounting should be made, the court could not tell but that Singizer was really indebted to Keeseman, who had also paid claims against the firm. Furthermore, to allow the administrator to get a dividend from Keeseman's estate, merely because the administrator had paid firm debts, would break the rule which appropriates a partner's personal assets to the payment of his private creditors.

Compare the foregoing case with *McCormick's Appeal* (1866), 55 Pa. 252. McCormick had been in partnership with William Hayes, who died. The firm was insolvent, as also was Hayes. Hayes owed the firm about \$16,800, and McCormick owed it about \$11,200. McCormick, as surviving partner, made an assignment of the firm property for the benefit of firm creditors. The assignee claimed a dividend out of Hayes' estate upon the amount which Hayes owed the firm. Hayes' private creditors objected that this was really an attempt by firm creditors, through their representative, the assignee, to share in Hayes' separate estate. The court refused to allow a dividend on the entire claim of about \$16,800; for

the net amount which Hayes owed the firm upon an adjustment of accounts was only about \$5,600, the excess of his indebtedness above McCormick's. As this sum, \$5,600, was due the firm, Hayes owed it not only to McCormick, but also partly to himself as equal partner with McCormick. His actual indebtedness to McCormick was, therefore, only about \$2,800. The court permitted the assignee to take advantage of this claim of McCormick's, representing the balance due him personally by Hayes upon the settlement of the firm accounts. The assignee's claim upon which a dividend was allowed him out of Hayes' separate estate was, therefore, reduced to \$2,800.

No fixed rule can be laid down regarding the charging of interest. Sometimes the courts hold a partner liable for interest on advances to him from the firm treasury or on contributions which he has failed to make at the time agreed, and in other cases they decide that the circumstances excuse him from the payment of interest. Sometimes interest is allowed on moneys contributed to the firm, but, as a rule, contributions of capital do not carry interest, for the partners are supposed to expect profits in return for such contributions, rather than to put them on the basis of loans. Of course, where there has been an express agreement on the subject, that will govern. There is no fixed rule governing the expenses of the accounting itself. Usually they are charged to the partnership. If the gross negligence or fraud of one partner has alone necessitated the accounting, he ought to bear the entire cost.

CHAPTER XXIV.

PARTNERSHIPS FORMED UNDER PENNSYLVANIA STATUTES.

In the last three chapters we have been considering the ordinary old-fashioned form of partnership. This kind of partnership may be varied to suit different requirements, but one feature is always present, namely, that every member of the firm is ultimately responsible without limit for firm debts, unless the creditor who seeks to charge him has made a con-

tract releasing him from personal liability. This holds true even in the case of "dormant" or "sleeping" partners, who take no part in managing firm affairs, and are not known to the world as members of the firm. The sleeping partner is interested in the firm as a co-principal, and is responsible for its debts by virtue of the rule mentioned in the twentieth chapter, that an undisclosed principal is liable to third parties who were not even aware of his existence when they contracted with his agent. The only point of difference between the liability of an active partner and that of a sleeping partner is that the latter on retiring from a firm escapes responsibility for the firm's subsequent debts, even though he does not give notice of his retirement. The necessity for such notice cannot exist in his case, for those who deal with the firm are ignorant of his connection with it, and are unable to invoke the doctrine of estoppel. This doctrine, as explained in the twenty-second chapter, is what requires the ordinary partner to give notice when he withdraws from his firm.

(A) *Special partners under the act of March 21, 1836.*

Modern business conditions demand a form of partnership for use in some cases which differs from the ordinary sort. Many capitalists do not want to risk their entire fortune in the outcome of a single business venture, so the feature of limited liability is provided for in several Pennsylvania statutes. The law first introducing this feature was enacted in 1836. The act was an experiment, and was hedged around with strict provisions. In consequence of the strictness of this act, many partners who failed to comply exactly with its terms have been held personally liable for firm debts, although they fancied themselves safe. For instance, the act forbids those special members of a firm who desire immunity from personal liability to transact business and sign for the partnership. *Only the general members who are personally responsible should act on behalf of the firm.* In the case of *Richardson v. Hogg* (1861), 38 Pa. 153, it appeared that Richardson had been in partnership with a man named John Lemon, under the firm name of

John Lemon. Hogg tried to hold Richardson liable for a firm debt, but Richardson claimed protection under the act of 1836. Hogg showed that the firm agreement provided that Richardson's son should keep the books and supervise the affairs during the firm's continuance, at a yearly salary of \$1,500, and that Lemon was to sign no check, note or other contract to pay money without young Richardson's approval. The court held that this was a fatal defect in the partnership articles, for Richardson virtually had control of the firm moneys through his son. The effect of this arrangement was to make Lemon a bare clerk instead of the managing general partner, the only one whom the act allowed to transact firm business. Hogg was thus enabled to hold Richardson personally liable, the firm having failed.

The act of 1836 aimed to substitute for the special partner's personal liability a fund of capital contributed by him. He was regarded as an outside capitalist who, taking no active part in the firm's affairs, drew his share of profits by reason of his contribution to its treasury.

Public notice should be given, in the manner hereafter described, of the amount of this contribution, which the act of 1836 required to be made in cash in order to prevent the public from being misled by watered capital. The act of March 30, 1865, however, permits any special partner to make his contribution in cash, goods or merchandise, provided that when it is made in goods or merchandise, the same shall first be appraised under oath by an appraiser appointed by the Common Pleas Court of the county where the partnership is to be conducted. The act of 1865 provides further that the nature and value of the said goods and merchandise shall be fully described in the certificate required by the act of 1836. This certificate must contain: (1) the firm name, (2) the general nature of the firm business, (3) the names and residences of the general and special partners, distinguishing those who are special from those who are general, (4) the amount of capital contributed by each special partner, (5) the time when the partnership is to begin and the time when it is to terminate. This certificate must be signed and acknowledged by all the

members in the same way that deeds are acknowledged. It should be recorded and filed in the office of the Recorder of Deeds of the county where the firm's principal place of business is located. If the firm has places of business in other counties, a transcript of the original certificate, certified by the recorder in whose office it was filed, must be filed and recorded in such other counties. As soon as any such certificate is filed, its terms must be published every week for at least six weeks in two newspapers designated by the Recorder of Deeds and published in the county where the business is carried on. Thus, if the firm transacts business in two counties, publication must be made in both, otherwise the special partner is deprived of his immunity. The exact wording of the certificate need not be followed in the newspaper advertisements, but the information required to be in the certificate about the five points mentioned above must also be given in the publication, except the following two particulars: first, the names and residences of the special partners may be omitted from the advertisement, and, second, the exact amount contributed by each special partner need not be stated in the advertisement, if the partners prefer merely to name the aggregate amount of capital contributed by all the special partners. In some counties the local rules of court require additional advertising.

At the time of filing the original certificate, an affidavit of one or more of the general partners must also be filed in the office of the Recorder of Deeds of the county where the firm's principal place of business is located, stating that the sums of money specified in the certificate as having been contributed by each of the special partners has actually, and in good faith, been paid in cash. If any false statement appears in the certificate or affidavit, all the partners are liable for firm engagements, as general partners. If the act of 1836 is properly complied with, the special partners do not stand to lose anything in the event of the firm's failure except the amount of their subscriptions.

The same act directs that every renewal or continuance of the partnership beyond the time originally fixed for its duration shall be certified, acknowledged and recorded, and an

affidavit of a general partner shall be made and filed, and notice shall be given in the manner required for its original formation. The necessity of exact compliance with the letter of this act and its supplements also is shown in *Blumenthal Bros. & Co. v. Whitaker* (1895), 170 Pa. 309. Creditors of Haines & Co. sought to hold Whitaker, an alleged special partner, liable as a general partner on the ground that the certificate filed with the Recorder of Deeds did not exactly comply with the statutory requirements. The firm of Haines & Co. contained two "special partners," Whitaker and Bacon; the certificate filed with the Recorder stated that "the amount of the capital stock contributed by said special partners is \$200,000, *one-half thereof being in goods and merchandise.*" The act of 1865 allows special partners to make their contribution to the capital stock of the firm in goods or merchandise, provided, however, the *nature and value of the goods be fully set forth in the certificate*—an important provision, designed to give the public means of knowing precisely what are the assets of the firm with which it is invited to deal. Now, clearly enough, the statement in the certificate was in this case no full statement of the nature and value of the goods contributed. A year later, when the partnership was renewed, the following statement was made in the renewal certificate: "The amount of capital originally contributed by each of the said special partners to the common stock was \$100,000, one-half thereof being in cash, and the other half thereof in goods and merchandise, making the aggregate amount of capital contributed by them \$200,000, as designated in the said original certificate, and the same remains unimpaired and undiminished as their contribution to the present renewal of the partnership." The court, reasoning that the failure of the original certificate exactly to comply with the requirements of the act of 1865 prevented the creation of a special partnership in the first instance and that a renewal of the partnership a year later could not cure the defect held Whitaker liable as a general partner. Even if the original certificate had been drawn in exact compliance with the act, the renewal certificate, simply referring in general terms to the original certificate and not

detailing the "nature and value of the goods," must have been held insufficient.

Coffin's Appeal (1884), 106 Pa. 280, shows that the act of 1836 is intended to compensate firm creditors who cannot hold a special partner liable by requiring that *the firm capital shall be really increased by the amount of the special partner's contribution*. Albert H. Mershon was a special partner in a firm which failed. He had borrowed the capital, \$12,000, contributed by him; and given his notes to the lenders. Six months after the partnership was formed, Mershon's notes were exchanged for notes signed by the general partners. Some creditors of the firm contested the right of the persons who had loaned the sum of \$12,000 to proceed against the firm assets. The court upheld this contention, for the practical result of letting the partnership assume Mershon's debt would be to make his contribution worthless. When notice is given under the act of 1836 by limited partnerships that the special partner has contributed \$12,000, the public are informed that the firm's capital is greater by that amount. If the firm afterwards assumes the special partner's personal obligation of repaying the money to those from whom he borrowed it, the net result is nothing, for the firm liabilities are increased to the same extent as its assets.

There are many provisions of the act of 1836 which need not be treated here. There are also a number of other acts passed in later years to amend and amplify this statute. The following paragraphs will complete what has been said above in the way of giving a general view of the act of 1836 and of subsequent supplementary legislation:

Limited partnerships for the transaction of any agricultural, mercantile, mechanical, mining and transporting of coal, or manufacturing business, within this state, may be formed by two or more persons, upon terms herein prescribed; but the provisions of this act shall not be construed to authorize any such partnership for the purpose of banking or making insurance. 1836, March 21, sec. 1.

Every *alteration* which shall be made in the names of the partners, in the nature of the business, or in the capital or

shares thereof, or in any other matter specified in the original certificate, shall be deemed a dissolution of the partnership, and every such partnership which shall in any manner be carried on after any such alteration shall have been made shall be deemed a general partnership, unless renewed as a special partnership. 1836, March 21, sec. 12.

The capital of the firm may be increased, either by taking in new special partners, or new subscriptions of capital from the partners previously in the firm, such increase being made in pursuance of the consent of the partners, as expressed in the original articles of partnership, or in any other subsequent instrument of writing. Every such increase of capital shall be duly acknowledged, certified and recorded; but no neglect in recording the certificate of any such increase of capital, or of any sale or transfer of the interests or shares of the special partners, or any of them, shall be construed to operate as a dissolution of the firm, or to make the special partners liable as general partners. 1858, April 21.

Business to be conducted under a firm name.—The business of the partnership shall be conducted under a firm name, in which the names of the general partners only shall be inserted, without the addition of the word "*company*," or any other general term, and if the name of any special partner shall be used in such firm name, with his privity, he shall be deemed a general partner. 1836, March 21, sec. 13. *Sec, however, the next two paragraphs.*

The firm name.—The business of the partnership shall be conducted under a firm name, in which the names of all the general partners shall be inserted, except, that when there are more than two general partners, the firm name may consist of either two of such partners, with the addition of the words "*and company*," but the said partnership shall put up, upon some conspicuous place on the outside, and in front of the building in which it has its chief place of business, some sign, on which shall be painted, in legible English characters, all the names, in full, of all the members of said partnership, stating who are general, and who are special, partners. 1865, March 30, sec. 2.

Firm name may include the words "and company."—The firm name of any limited partnership may consist of the name of any general partner, with the addition of the words "and company," notwithstanding the name of such general partner may be common to him and any special partner; but the said partnership shall put up the sign required by the second section of the act approved March 30, 1865, to which this is a supplement. 1868, Feb. 21.

Suits.—Suits in relation to the business of the partnership may be brought and conducted by and against the general partners, in the same manner as if there were no special partners. 1836, March 21, sec. 14.

Liability for previous debts. Interest and dividends.—No part of the sum which any special partner shall have contributed to the capital stock shall be liable for any debts previously contracted by the general partners, nor shall any part of such sum be withdrawn by him, or paid or transferred to him in the shape of dividends, profits or otherwise, at any time during the continuance of the partnership; but any partner may annually receive lawful interest on the sum so contributed by him, if the payment of such interest shall not reduce the original amount of such capital, and if, after the payment of such interest, any profits shall remain to be divided, he may also receive his portion of such profits. 1836, March 21, sec. 15.

Original capital not to be reduced.—If it shall appear that, by the payment of interest or profits to any special partner, the original capital has been reduced, the partner receiving the same shall be bound to restore the amount necessary to make good his share of capital, with interest. 1836, March 21, sec. 16.

Rights of a special partner.—A special partner may, from time to time, examine into the state and progress of the partnership concerns, and may advise as to their management, but he shall not transact any business on account of the partnership, nor be employed for that purpose as agent, attorney or otherwise; if he shall interfere contrary to these provisions, he shall be deemed a general partner. 1836, March 21, sec. 17.

Liability of general partners.—The general partners shall

be liable to account to each other and to the special partners, for the management of their concern, both in law and equity, as other partners now are by law. 1836, March 21, sec. 18.

Creditors' priority.—In case of the insolvency or bankruptcy of the partnership, no special partner shall, under any circumstances, be allowed to claim as a creditor, until the claims of all the other creditors of the partnership shall be satisfied. 1836, March 21, sec. 23.

Dissolution.—No dissolution of such partnership, by the act of the parties, shall take place previous to the time specified in the certificate of its formation, or in the certificate of its renewal, until a notice of such dissolution shall have been filed and recorded in the recorder's office in which the original certificate was recorded, and published once in each week, for four weeks, in a newspaper printed in each of the counties where the partnership shall have places of business. 1836, March 21, sec. 24.

Transfer of interest of general partners.—A general partner in any limited partnership may, with the assent in writing of his partner, by deed duly acknowledged and recorded, or by last will and testament in writing, sell, assign, dispose of or bequeath his interest in such limited partnership; and when such general partner dies without having disposed of his interest in such limited partnership, his administrator or executor may, in like manner, sell, assign and transfer his interest therein for the benefit of his estate, and on every such sale, transfer or bequest, a corresponding alteration shall be made in the firm name under which the business of such partnership is conducted and the same shall be forthwith acknowledged, certified, recorded and published in the same manner as is provided by law in the case of the original formation of the partnership. 1838, April 16, cl. 10.

Special partner may dispose of his interest.—A special partner, with the assent of his partner in writing, first had and obtained, may sell or assign his interest in a limited partnership, without causing thereby a dissolution of the partnership. 1838, April 16, cl. 11.

Sale of interest.—The consent of the partners to a

sale or transfer, by either the general or special partners, of their respective interests in the partnership, in pursuance of the resolution of April 16, 1838, may be given in advance, either in the original articles of partnership or other like instrument; and a sale or transfer of any part or share of the interest in the firm of any partner, if made in pursuance of the articles of co-partnership, or previously expressed consent of the partners as aforesaid, shall be equally valid as a sale of the whole interest of any one or more of the partners; and it shall further be lawful for the general partner or partners, or either of them, to purchase part or the whole of the interest or shares of one or more of the special partners. 1858, April 21, sec. 2.

Insolvency of special partner not to dissolve firm.—The insolvency of any special partner shall not cause a dissolution of the limited partnership, but his interest therein shall be sold by his assignees for the benefit of his creditors. 1838, April 16, cl. 12.

Rights of executors and administrators.—When any special partner shall die, without having disposed of his interest in the limited partnership, his executor or administrator may either continue his interest therein for its unexpired term, for the benefit of his estate, or may sell the same at public auction, under the direction of the orphans' court of the county in which the principal place of business of such partnership may be, in the same manner as the estates of intestates are now by law sold; testamentary dispositions, in writing, of the interest of special partners, may also be made; the decease of special partners shall not dissolve such limited partnership, unless by the agreement between the parties it is provided that such decease shall have that effect. 1838, April 16, cl. 13.

Formalities attending alteration.—Every alteration in such limited partnership, according to the provisions of this resolve, shall be notified to the general partner, and shall be duly acknowledged, certified and recorded, as in the case of the original formation of such partnership. 1838, April 16, cl. 14.

The act of 1836 also provides that if any sale, assignment or transfer of partnership property is made while the partnership is insolvent, or in contemplation of insolvency, with the intention of giving an unlawful preference to any partnership creditor or any separate creditor of one of the partners over the other firm creditors, and any special partner concurs in the attempt to give such a preference, the special partner shall be liable as a general partner.

(B) *Limited partnership associations under the act of June 2, 1874.*

The act of 1836, which has just been considered, secures limited liability only to those who do not actively transact business for the firm. The act of 1874 enables all the members, active and inactive, to obtain immunity from personal liability for firm debts. This act is not so strict as the act of 1836, but the members should be careful, nevertheless, to see that its terms are carried out fully. The importance of this is seen in the case of *Hill v. Stetler* (1889), 127 Pa. 145. The recorded statement of a partnership organized under the act of 1874 set out that the total amount of capital was \$25,000, "payable in lawful money on the execution hereof," but the association began business with no part of its capital paid in. The statement mentioned that S. N. Stetler and E. N. Fuller had subscribed for \$8,000 apiece, and that R. W. Archbald had subscribed for the balance of the capital, \$9,000. No subscription list book was opened, as required by the act. Five months after the association was formed, Theodore Strong bought ten of its shares, paying their full par value, \$1,000, into the treasury. The concern failed, and certain creditors sought to hold the members personally liable. The court decided that they had not brought themselves within the protection of the act of 1874, although they probably imagined that they had complied with it. The following quotations are from the court's opinion:

"The act provides for the protection from personal liability of those who 'subscribe and contribute' a capital to be employed

in any lawful business. The 'capital' is staked upon the success of the business, but because the amount of the capital appears upon the statement on record and the 'subscription list book' on the desk of the association, all who have occasion to deal with it may know the amount of actual capital within reach, and determine to what extent the association is entitled to credit. But persons who subscribe yet never contribute, and who, by failing to keep a 'subscription list book' withhold from the public all means of knowing the truth, cannot be within the protection of the act. They really put nothing into the enterprise except the credit of a capital which is actually withheld. They mislead the public and induce confidence to which they are not entitled.

"In the case of business corporations, the certificate that at least ten per cent of the subscribed capital has been paid in goes to the governor, and he then issues letters-patent, which impart life to the corporation. In the case of joint-stock associations, the members are trusted by the law to certify directly to the public without the intervening agency of the governor, and thus to give life to their own creature. Under such circumstances the courts should require absolute good faith and an honest compliance with the law from those who claim exemption from individual liability as members of a joint-stock association. If no capital has been put into the concern, no actual cash with which to begin business, it has no right to begin business. The subscribers have no right to record the certificate, and to do so is a fraud. We do not say that the entire capital must be paid down. The law does not say so, but seems to contemplate a payment by instalments. In analogy to the business corporations of the state, ten per cent of the subscribed capital would seem to be the minimum amount to be actually provided for and paid into the treasury before the recording of the certificate, which, as we have already said, should show the times of subscription truly, and should be complied with fully and honestly before it goes upon record."

Strong, one of the four defendants in this case of *Hill v. Stetler*, had not been one of the original subscribers, and it was urged that he should not be made liable for their misrep-

resentations. The court pointed out that as he had bought his ten shares directly from the company, he should have realized that the recorded statement to the effect that the entire capital had been already paid in was false. He was bound to inquire into the manner in which the association had been organized, and his position was the same as if he had bought an interest in an ordinary old-fashioned partnership. He did not become liable for debts contracted before he acquired an interest in the concern, but for debts contracted afterwards he was liable as a partner, along with his three associates.

In the following paragraphs are given the most important sections of the act of 1874, together with some sections from certain amending acts:

Formation of limited partnership associations.—When any three or more persons may desire to form a partnership association, for the purpose of conducting any lawful business within the United States or elsewhere, whose principal office or place of business shall be established and maintained within this state, by subscribing and contributing capital thereto, which capital shall alone be liable for the debts of such association, it shall and may be lawful for such persons to sign and acknowledge, before some officer competent to take the acknowledgment of deeds, a statement in writing, in which shall be set forth the full names of such persons, and the amount of capital of said association subscribed for by each; the total amount of capital, and when and how to be paid; the character of the business to be conducted and the location of the same; the name of the association with the word "*limited*" added thereto as part of the same; the contemplated duration of said association, *which shall not in any case exceed twenty years*, and the names of the officers of said association, selected in conformity with the provisions of this act; and any amendment of said statement shall be made only in like manner, which said statement and amendments shall be recorded in the office of the recorder of deeds of the proper county. 1874, June 2, sec. 1.

.. *Liability of the members.*—The members of any such partnership association shall not be liable under any judgment,

decree or order which shall be obtained against such association, or for any debt or engagement of such company, further or otherwise than is hereinafter provided; that is to say, if any execution, either at law or in equity, shall have been issued against the property or effects of the company, and if there cannot be found sufficient thereof, whereon to levy or enforce such execution, sequestration or other process, then such execution, sequestration or other process may be issued against any of the members to the extent of the portions of their subscriptions, respectively, in the capital of the association not then paid up: Provided always, That no such execution shall issue against any member, except upon an order of court or of a judge of the court in which the action, suit or other proceeding shall have been brought or instituted; and the said court or judge may compel the production of the books of the association, showing the names of the members thereof and the amount of capital remaining to be paid upon their respective subscriptions, and from them, or other sources of information, ascertain the truth in regard thereto, and may order execution to issue accordingly; and the said association shall be and it is required to keep a subscription list book for that purpose, and the same shall be open to inspection by the creditors and members of the association at all reasonable times. 1874, June 2, sec. 2.

Word "limited" to be used.—The word "limited" shall be the last word of the name of every partnership association, formed under the provisions of this act; and every such association shall paint or affix, and shall keep painted or affixed, its name on the outside of every office or place in which the business of the association is carried on, in a conspicuous position, in letters easily legible, and shall have its full name mentioned in legible characters in all notices, advertisements and other official publications of such association, and in all bills of exchange, promissory notes, notes, checks, orders for money, bills of lading, invoices, receipts, letters and other writings used in the transaction of the business of the partnership association: Provided, That the omission of the word "limited" in the use of the name of the partnership association

shall render each and every person participant in such omission, or knowingly acquiescing therein, liable for any indebtedness, damage or liability arising therefrom. 1874, June 2, sec. 3.

Transfer of a member's interest.—Interests in such partnership associations shall be personal estate, and may be transferred, given, bequeathed, distributed, sold or assigned, under such rules and regulations as such partnership associations shall from time to time prescribe by a vote of a majority of the members in number and value of their interests; and in the absence of such rules and regulations, the transferee of any interest in such association shall not be entitled to any participation in the subsequent business of such association, unless elected to membership therein, by a vote of the majority of the members in number and value of their interests. And any change of ownership, whether by sale, death, bankruptcy or otherwise, which occurs in the absence of any rules and regulations of such associations regulating such transfer, and which is not followed by election to membership in such associations, shall entitle the owner or transferee only to the value of the interest so acquired at the date of acquiring such interest, at a price and upon terms to be mutually agreed upon, and in default of such agreement, at a price and upon terms to be fixed by an appraiser to be appointed by the Court of Common Pleas of the proper county, on the petition of either party, which appraisal shall be subject to the approval of said court. 1885, June 25, sec. 1.

Meetings, officers and liabilities.—There shall be at least one meeting of the members of the association in each year; at one of the meetings there shall be elected not less than three or more than five managers of the association, one of whom shall be the chairman, one the treasurer and one the secretary, or the office of both treasurer and secretary may be filled by one person, who shall hold their respective offices one year, and until their successors are duly installed. The board of managers are authorized to fix the salary and compensation of such officers, and the salary and compensation of other employees, but the president, secretary and treasurer shall not receive as salary or compensation, after such association has

been in existence for five years, a sum in the aggregate greater than the amount of net earnings actually earned during the year preceding, unless by the consent of all the members of the association; and the salary of the president, secretary and treasurer shall be fixed for the ensuing year, by a two-thirds vote of the value of interest present at the annual meeting of the association, and after the annual report has been made. No debt shall be contracted or liability incurred for such association, except by one or more of the managers, and no liability greater than five hundred dollars, except against the person incurring it, shall bind the association, unless reduced to writing and signed by at least two managers. 1889, May 10, sec. 1.

Dividends.—The association may from time to time divide the profits of its business in such manner and in such an amount as the majority of its managers may determine, which profits so divided shall not at the time diminish or impair the capital of the said association; and anyone consenting to a dividend which shall diminish or impair the capital shall be liable to any person or persons interested or injured thereby, to the amount of such diminution or impairment. 1874, June 2, sec. 6.

Loan of credit, name or capital forbidden.—It shall not be lawful for such association to loan its credit, its name or its capital to any member of said association, and for a loan to any other person or association the consent in writing of a majority in number and value of interest shall be requisite. 1874, June 2, sec. 7.

Dissolution.—Such association may be dissolved:

I. Whenever the period fixed for the duration of the association expires.

II. Whenever, by a vote of a majority in number and value of interest, it shall be so determined, and notice of such winding up shall be given by publication in two newspapers, published in the proper city or county, at least six consecutive times, and immediately upon the commencement of said advertising, said association shall cease to carry on its business, except so far as may be required for the beneficial winding up thereof. 1874, June 2, sec. 8.

Three liquidating trustees.—Three liquidating trustees, not more than two of whom shall have been a manager of the association so dissolved and in liquidation, shall be elected by the members of the association, who shall have full power to settle the affairs of the association, and distribute the assets thereof, after the payment of its debts, among the members, under the direction of the Court of Common Pleas of the proper county. 1889, May 10, sec. 2.

Distribution of property.—When any such partnership association shall be dissolved by the voluntary action thereof, its property shall be applied and distributed as follows:

I. To the payment of all debts for wages of labor.

II. To the satisfaction of its other liabilities and indebtedness.

III. After payment thereof, the same shall be distributed to and among the members thereof, in proportion to their respective interests. 1874, June 2, sec. 9.

A common seal may be used.—Whenever any association, formed under the act to which this is a supplement, shall have occasion to execute any deed of conveyance, or bonds with or without coupons, and mortgages, to secure, purchase or borrow moneys, such association shall have a right to adopt and use a common seal, and to acknowledge such instruments or writings by their chairman and secretary. 1875, February 18, sec. 1.

Contributions to capital may be made in real or personal property.—It shall and may be lawful for any person desiring to form a partnership association, under the act to which this is a supplement, to make contribution to the capital thereof in real or personal estate, mines or other property, at a valuation to be approved by all the members subscribing to the capital of such association: Provided, That in the statement required to be recorded by the first section of the said act, subscriptions to the capital, whether in cash or in property, shall be certified in this respect according to the fact; and when property has been contributed as part of the capital, a schedule containing the names of the parties so contributing, with the description and valuation of the property so contributed, shall be inserted. 1876, May 1, sec. 1.

Association shall hold realty, and shall sue and be sued, in association name.—All real estate owned or purchased by any association heretofore created, or which may be hereafter created, under and by virtue of the act to which this is a supplement, shall be held and owned, and conveyance thereof shall be made, in the association name; the said association shall sue and be sued in their association name. 1876, May 1, sec. 3.

For the method of serving writs upon partnership associations, see the act of April 3, 1903.

(C) *Limited partnership associations under the act of May 9, 1899.*

The act of May 9, 1899, as amended by that of July 9, 1901, provides a system for organizing limited partnerships, which are largely like those formed under the act of 1874. They possess some advantages over those formed under the act of 1874. The word "limited" need not be part of the firm name in concerns organized under the act of 1899. This act, however, directs that no firm name shall be adopted which will include the name of any partner whose liability is intended to be limited, unless there shall be added the word "*registered*." The act of 1899 enables some members to limit their liability, while others are general partners. This could not be accomplished under the act of 1874, which shielded all the partners equally from personal responsibility. The advantage of the later statute lies in the fact that it may, perhaps, be desirable to gain credit for certain partnership associations by having some of their members liable as general partners.

A comparison of the partnership association acts with the corporation acts mentioned in the next chapter will reveal the substantial identity of the two kinds of organization. The difference between them is largely nominal. Some fear is felt, however, lest the courts of our sister states may not always be inclined to recognize the partnership acts which have been treated in this chapter. Suppose a limited association formed under the act of 1899 owes debts, and suits are brought thereon in another state against the members. If the concern were

insolvent, the members would be quick to assert that they were not individually liable. It is, perhaps, possible that the local courts, especially in the South and West, might be disposed to disregard the protection sought to be obtained under our Pennsylvania statutes. On the contrary, it is well settled that a corporation charter protects the members in any state.

The similarity between partnership associations and corporations has led to the passage of legislation which puts the two kinds of organization on much the same basis as respects the payment of bonus and taxes. This subject is treated in Chapter XXXIV, and an act concerning the payment of bonus is set forth at the end of the present chapter. Special partnerships under the act of 1836 are not affected by this legislation. The following paragraphs contain some of the important provisions of the act of May 9, 1899, and the act of July 9, 1901, referred to above.

Formation of partnerships with limited liability.—Where two or more persons may desire to associate themselves in partnership for the purpose of conducting any kind or kinds of business, trade or occupation, except the construction and operation of electric light and power companies, banking or trust companies, artificial or natural gas companies, water companies, railroad, street passenger railway or traction companies, within this state or any portion of the United States or elsewhere, whose principal office or place of business shall be specified in the way and manner hereinafter set forth as being intended to be established and maintained within this state, and may desire to limit the liability of one or more or all of the partners for the debts of the partnership to the amount of the capital subscribed by such partner or partners, respectively, it shall and may be lawful to do so in the manner following, to wit:

Said partners, so desiring to associate themselves, shall subscribe the articles of partnership wherein shall be stated the name and style of the partnership, its purposes and duration, the county wherein its principal office or place of business is to be located, the names of the several partners, and the amount of capital to be subscribed by each partner and when

and how the same is to be paid, and the names of the partners, one or more or all, whose liability is to be limited to the amount subscribed by each to the capital. Such articles of partnership shall be acknowledged before some officer competent to take the acknowledgment of deeds, and shall be recorded in the office of the Recorder of Deeds of the county in which is located the place designated as the principal office or place of business. Amendments of said articles of partnership shall be made in like manner, and shall be effective only when recorded in the office of the said Recorder of Deeds. A copy of said articles of partnership, and of all amendments thereto, duly certified by the Recorder of Deeds, shall also be filed, within thirty days after the recording of said articles or amendments in said Recorder's office, in the office of the Secretary of the Commonwealth. The business of the partnership may be commenced after the articles of partnership have been left for record in the office of the Recorder of Deeds. 1901, July 9, sec. 1.

Notice of formation of partnership.—Notice of the formation of the partnership shall be published in a newspaper of general circulation in the county wherein is located the place designated as the principal office or place of business. This notice shall be published once a week for three weeks. The first publication shall appear not later than one day following the filing of the articles of partnership in the office of the Recorder of Deeds. This notice shall state the name, style and general purpose of the partnership, the names of the partners, the amount of capital subscribed for by each partner, and when and how the amount of each subscription is to be paid. It shall also state the fact that the liability of one or more or all of the partners is limited in accordance with the statute, and that the articles of partnership have been left for record in the office of the Recorder of Deeds. If a time be fixed in the articles of partnership for its duration, such time shall also be stated in the said notice. No name or style of partnership shall be adopted which will include the name of any partner whose liability is intended to be limited, unless there shall be added the word "registered." 1899, May 9, sec. 2.

Liability and powers of members of partnership.—No

member of any such partnership thus formed, recorded and published, whose liability is stated as intended to be limited in the manner hereinbefore set forth, shall be liable for its debts under any circumstances saving to the extent or amount of his or her subscription, with interest on unpaid subscriptions from the date or dates at which the same became actually due and payable. Payment of the amount of the subscription of such member of the partnership, with interest as aforesaid, shall exonerate such partner from all further liability. *A partner or partners whose liability is thus limited shall not be precluded from transacting business with or for the partnership.* 1899, May 9, sec. 3.

Control of the business.—The partners may provide that certain only of the members shall have active charge of the business and be authorized to enter into contracts, undertakings, or engagements whereby the partnership shall be held liable, and may change the same as they see fit. It shall be optional with the partnership whether such provision shall or shall not be made. It shall also be optional with the partnership, if such provision be made, to state the same in the original articles of partnership, or in amendments thereto, or in any statement subscribed by the partners. If the partners shall desire, any such statement may be acknowledged and may be recorded in the office of the said Recorder of Deeds. The partnership may at its option adopt and use a common seal. 1899, May 9, sec. 4.

List of partners to be posted in principal office.—It shall be the duty of the said partnership to keep posted in the place designated as its principal office, or place of business, in some place therein accessible to the public during business hours, a plainly written or printed list of the partners with the amount of the capital subscribed by each, the amount paid in by each partner, and in the case of any partner whose liability is limited the words "Limited Liability" shall be added to his name where it appears in such list. This notice shall also state the volume and page of the record of the articles of partnership in the office of the Recorder of Deeds. 1899, May 9, sec. 5.

Reference to limited liability on signs, billheads, etc.—

If on the signs used by the partnership, or if on any bill-heads, letter-heads, or other publications of the partnership, the names of the several partners should be stated, the words "Limited Liability" shall be added to the name of the partner whose liability is limited in the way herein provided. 1899, May 9, sec. 5.

Violation of section 5 a misdemeanor.—A violation of any of the provisions of this section shall be a misdemeanor. Each member of a partnership who shall participate in such violation shall be liable to prosecution for such misdemeanor, and upon conviction shall be sentenced to pay a fine of not less than one hundred dollars, and not more than five hundred dollars. 1899, May 9, sec. 5.

Transfer of a member's interest in partnership.—Interest in said partnership shall be personal estate, and may be transferred, given, bequeathed, distributed, sold or assigned, under such rules and regulations as may from time to time be prescribed by a vote of the majority in number and interest of the partners; but, in the absence of such rules and regulations, the transferee of any such interest shall not be entitled to participation in the subsequent business of the partnership unless elected as a partner therein by a vote of the majority in number and interest of the remaining partners. Any change of ownership, whether by sale, death, bankruptcy or otherwise, which shall occur in the absence of such rules and regulations, and which shall not be followed by election to membership, shall entitle the owner or transferee to the book value of the interest so acquired, as ascertained and fixed, as hereinafter provided, at the last period preceding the date at which the member parted with or lost his interest, with interest from such date. 1899, May 9, sec. 7.

Ascertainment of book value of interest.—It shall be the duty of the partnership at the close of each calendar year to ascertain and fix the book value of the several interests, a copy of which statement shall be delivered to each partner, and this settlement shall be conclusive and final upon all members of the said partnership, and upon all subsequent owners or transferees of any interest. 1899, May 9, sec. 7.

Transfer or death not to dissolve partnership.—The transfer of any interest, however occurring, shall not dissolve the partnership, nor shall said partnership be dissolved by reason of the death of one or more of the partners, unless the articles of association shall prescribe to the contrary. In case of a change in the members of the partnership by reason of death, transfer or otherwise, it shall not be necessary to make any publication of the fact thereof. 1899, May 9, sec. 7.

Expiration and renewal of partnership.—If at the expiration of the time fixed for the duration of the partnership, if any time be so fixed, the persons then constituting the partnership shall desire to renew the same, they may do so by articles specifying the fact of such renewal and the length of time fixed for the duration of the new partnership. Such agreement of renewal shall be recorded and published in the way and manner hereinbefore provided in the case of an original partnership. 1899, May 9, sec. 8.

Powers concerning real estate.—The partnership may take, hold, mortgage, encumber, lease or convey, in fee simple, or for any less estate, real estate or interests therein, in the firm name. The place of record of the articles of partnership shall be stated in all instruments of writing relating to real estate, but failure so to state shall not invalidate the instrument. Any instrument relating to real estate may be signed or sealed by one or more of the partners, for the partnership and in the partnership name, if the by-laws, rules or regulations shall so provide, but in case less than all the partners are vested with this power the fact shall be stated in the original articles of partnership, or in the amendments thereto, or in a statement duly signed and acknowledged by the partners and recorded in the office of the Recorder of Deeds. 1899, May 9, sec. 9.

Dissolution.—Partnerships may be dissolved at any time by a vote of the majority in number and interest of those who at such time shall constitute the partnership, unless the articles of association shall provide to the contrary. In case of dissolution for any cause, whether by expiration of the period fixed for the partnership or otherwise, notice thereof shall be published in the county designated as the place wherein the prin-

cial office or place of business is located, for six consecutive issues, and immediately upon the commencement of said advertising said partnership shall cease to carry on its business except so far as may be necessary for the beneficial winding up thereof. In case of dissolution, one or more liquidating partners shall be elected by a vote of the majority in interest of the partners, who shall have full power and be charged with the duty of settling the affairs of the partnership and distribution of the assets thereof after the payment of its debts among the partners in proportion to their interest. 1899, May 9, sec. 10.

Suits by and against partnership.—The partnership shall sue and be sued in the partnership name, and not by or in the individual names of the partners. 1899, May 9, sec. 11.

For the method of serving writs upon partnership associations, see the act of April 3, 1903.

(D) Bonus on capital.

Bonus on capital of partnership associations.—Any partnership association formed under the provisions of an act, entitled "An act authorizing the formation of partnership associations in which the capital subscribed shall alone be responsible for the debts of the association, except under certain circumstances," approved the second day of June, Anno Domini one thousand eight hundred and seventy-four, and any partnership formed under the provisions of an act, entitled "An act authorizing the formation of partnerships in which one or more, or all of the partners, may limit their liability for the debts of the partnership to the amount of capital subscribed by such partner or partners, respectively, and providing penalties for violation of its provisions," approved the ninth day of May, Anno Domini one thousand eight hundred and ninety-nine, shall pay to the State Treasurer, for the use of the commonwealth, a bonus of *one-third of one per centum upon the amount of capital stock* which said company or companies shall have at the time of formation of such partnership, and a like bonus on any subsequent increase thereof, and no company formed under the provisions of said acts shall go into opera-

tion or exercise any privileges until said bonus has been paid. 1901, May 8, sec. 1.

Receipt for bonus to be recorded with articles of association.—No articles of association, forming a partnership association under either of the acts aforesaid, or any amendment thereto increasing the capital thereof, shall be accepted for record by the Recorder of Deeds in any county in this commonwealth unless there be annexed thereto a receipt of the State Treasurer for the amount of bonus due under this act, said receipt to be made a part of the articles of association and recorded therewith. 1901, May 8, sec. 2.

Articles of association to be void unless bonus is paid.—Any company formed under the provisions of either of the foregoing acts, which shall not pay the bonus required by this act, the articles of association thereof shall be void and of no effect, and every person a party thereto shall be held liable as general partners. 1901, May 8, sec. 3.

See Chapter XXXIV, where the taxation of domestic and foreign partnership associations is treated.

PART III

CORPORATIONS

CHAPTER XXV.

THE FORMATION OF CORPORATIONS.

We have seen that the ordinary partnership is formed merely by the private agreement of its members, which may be expressed in writing or by word of mouth or even by conduct alone. In the preceding chapter we saw that in the case of statutory partnerships much formality is required. The articles of agreement must be prepared in a certain way, and must be filed and recorded so as to be accessible to the public. We come now to consider a method of organization whereby the associates secure from the public authorities a charter, which is a formal recognition by the state of their association. Originally no corporation was organized without a special act or grant from the public authorities, banding its members together under a common name, and conferring certain privileges upon them. The growth of business has led to the passage of general acts, under which any number of associations may be formed. We have seen that on June 2, 1874, the Legislature authorized the formation of partnership associations, all of whose members were to enjoy limited liability. That same year, on April 29th, a general corporation act was passed, under which most Pennsylvania corporations are now formed.

A corporation is defined as "a body consisting of one or more natural persons, established by law, usually for some specific purpose, and continued by a succession of members." The words "established by law" serve to distinguish a corporation from some of the statutory partnerships (which are like it in all practical features), since these words point to the fact

that a corporation receives a *charter* directly from the state, while the statutory partnerships are "established" by the members themselves. The charter of a corporation of the first class is in the shape of a single document signed by a judge. That of a corporation of the second class is in the shape of two documents, one called "letters patent," the other a "certificate of incorporation," and both signed by the Governor. As the charter consists of nothing but a solemn grant of authority for the associates and their successors to do business under certain terms as a body corporate or corporation, the distinction between corporations and many statutory partnerships is more shadowy than real. The definition indicates that a corporation may consist of only one person. While no Pennsylvania corporation can be formed by fewer than three persons, we shall see in the case of *Bridge Co. v. Traction Co.*, set forth at the beginning of Chapter XXIX, that all the stock of a corporation may, after its formation, be legally acquired by a single owner.

The act of April 29, 1874, permits a corporation to be formed by the voluntary association of five or more persons, and directs that each company organized under its terms shall have the following seven powers, unless otherwise specially provided:

(1) To have succession by its corporate name for the period limited by its charter, and when no period is limited thereby, or by this act, perpetually, subject to the power of the General Assembly, under the Constitution of this Commonwealth.

(2) To maintain and defend judicial proceedings.

(3) To make and use a common seal and alter the same at pleasure.

(4) To hold, purchase and transfer such real and personal property as the purposes of the corporation require, not exceeding the amount limited by its charter or by law.

(5) To appoint and remove such subordinate officers and agents as the business of the corporation requires, and to allow them a suitable compensation.

(6) To make by-laws not inconsistent with law, for the management of its property, the regulation of its affairs, and the transfer of its stock.

(7) To enter into any obligation necessary to the transaction of its ordinary affairs.

The act of 1874 divides corporations formed under it into two main classes, namely, those not for profit and those for profit. The first class, as enlarged by subsequent legislation, includes concerns organized for any one of the following fourteen purposes :

(1) The support of public worship.

(2) The support of any benevolent, charitable, educational or missionary undertaking.

(3) The support of any literary, medical or scientific undertaking, library association, or the promotion of music, painting or other fine arts.

(4) The encouragement of agriculture and horticulture.

(5) The maintenance of public and private parks, and of the facilities for skating, boating, trotting and other innocent or athletic sports, including clubs for such purposes, and for the preservation of game and fish.

(6) The maintenance of a club for social enjoyments.

(7) The maintenance of a public or private cemetery.

(8) The erection of halls for public or private purposes.

(9) The maintenance of a society for beneficial or protective purposes to its members from funds collected therein.

(10) The support of fire engine, hook and ladder, hose or other companies for the control of fire.

(11) For the encouragement and protection of trade and commerce.

(12) For the formation and maintenance of military organizations.

(13) For the maintenance of a society for the improvement of the streets and public places in any city, borough or township in this commonwealth.

(14) For receiving and holding property, real and personal, of and for unincorporated religious, beneficial, charitable, educational, and missionary societies and associations, and executing trusts thereof.

Few corporations of the first class have any capital stock, but the act of June 25, 1895, authorizes any such corporation

to issue stock not exceeding \$250,000 in shares of \$50 par value, if a majority of its members shall so ordain. The act prescribes certain formalities which must be followed. Corporations of the first class which issue stock are taxable like those organized for profit.

The second class of corporations includes those organized for a large number of different purposes which need not be enumerated, since the supplements to the act of 1874 have so widened its scope that almost every kind of corporation for profit may now be organized under it except as mentioned below. If you desire to organize for any lawful purpose not specifically provided for by any act of the Pennsylvania legislature, the act of July 9, 1901, enables you to form a corporation of the second class, in accordance with the terms of the 1874 corporation statute and its supplements. The wide scope of the act of 1901, however, is likely to be restricted by the interpretation of the courts.

There are certain kinds of business of a semi-public nature, such as that transacted by *railroad companies*, which require more state supervision than the ordinary private business, such as that of manufacturing or commercial companies. Apart from the general corporation act of 1874, and its supplements, are a number of distinct and *independent statutes* regulating the formation of these semi-public corporations. *Insurance companies* are specially provided for by the acts of May 1, 1876, July 9, 1897, and by other statutes, although certain insurance companies may be formed under the act of 1874. No company will be chartered to transact both fire and life insurance. Again, *street railway, elevated or underground railroad companies* are regulated by special acts. Likewise, *traction and motor power companies, ship-canal companies and natural gas companies*. Likewise, *banking and savings bank companies*. Likewise, *exhibition companies and institutions of learning* which confer degrees in art, science, philosophy, literature, law, medicine or theology. Likewise, certain *co-operative associations* formed under the act of June 7, 1887, for carrying on farming, manufacturing, commercial and certain other pursuits, and certain co-operative banking associations formed

under the act of May 18, 1893, for carrying on a banking business.

(A) *Formation of corporations of the first class.*

Corporations of the first class, which are not for profit, receive their charters from the state through the Courts of Common Pleas. Corporations of the second class receive their charters from the Governor, or the Executive Department, at Harrisburg. Some corporations are included in the first class, although organized for profit, as, for instance, *those which conduct public parks or baseball grounds or halls* to which admission is charged. The act of June 26, 1895, requires most college charters to be approved by a special council. Railroad companies and most of the other concerns listed in the preceding paragraph get their charters from Harrisburg. The application for the incorporation of a company of the first class is made to the Court of Common Pleas of the county where its principal business is to be transacted. It should be set forth on one side of a single sheet of paper or parchment, and should be subscribed by at least five persons, three of whom must be citizens of Pennsylvania. Three of the subscribers must swear to the application before a Pennsylvania notary public or before the Recorder of Deeds of the county where it is to be presented. The application is then filed in the Prothonotary's office, where it remains for at least twenty-one days, while public notice of the intention to apply for a charter is being advertised. This notice must be inserted in two newspapers of general circulation, printed in the proper county, once a week for three weeks, and must set forth briefly the character and object of the corporation to be formed, and the intention to apply for a charter. In some counties the local rules of court require additional advertising. This publication of notice gives those who may have objections to the granting of the application a chance to learn about it. When the required advertising has been completed, the application is entertained by the Court of Common Pleas, and is frequently referred to a master, for a full examination. When a master is appointed, he usually requires witnesses to

be produced before him, in order that he may satisfy himself that the application is for a proper purpose. Sometimes the court grants a charter outright, without referring the matter to a master or hearing the testimony of witnesses. The application should contain sufficient information to show that the object of the proposed corporation is such as to give the court jurisdiction, and enable it to grant a charter, and is not likely to be harmful to the public. It should contain also general information about the proposed method of running the corporation, in order to show in what officers control is to be lodged and what are to be the rights of members. It should also indicate how the corporation property is to be controlled. The act of 1874 allows any corporation of the first class to hold real estate up to an amount, the clear yearly value or income whereof shall not exceed \$20,000.

Assuming that an application satisfies the foregoing requirements, and that it is approved and signed by a judge of the court, the next step is to have it recorded by the Recorder of Deeds of the same county. Thereafter the associates should hold a meeting, formally accept the charter, and proceed regularly to transact business under it. Much of what is said towards the end of this chapter about the adoption of by-laws and subsequent steps, in the organizing of corporations of the second class, may be applied to corporations of the first class also.

(B) *Formation of corporations of the second class.*

The act of 1874 required five associates to join in applying for any charter. Only three are now necessary in the case of corporations for profit, at least two of whom must sign and swear to the application. The affidavit may be made before a notary. At least one of the subscribers must be a citizen of Pennsylvania. Nobody should sign an application merely in order to complete the required number of incorporators, since if he is afterwards sued for the amount of his pretended subscription, he will not be allowed to show that it was not meant to bind him. Furthermore, he may cause trouble to the other associates, if he is so disposed, as is evident from *Rowley's Ap-*

peal (1886), 115 Pa. 150. William Tillyer filed a bill in equity to compel a certain corporation to admit him as a stockholder. The defense was that two persons owned the entire stock, and that the other incorporators, one of whom was Tillyer, had no interest in the concern. The Supreme Court declared that it would be wrong to let these two persons, who asserted that they were the only real stockholders, repudiate the solemn affidavit made by them in obtaining the charter. Accordingly, it was decreed that the company issue and deliver to Tillyer a certificate for the number of shares subscribed for by him in the application, upon his payment of their par value.

The application certificate should set forth seven different matters, as follows: first, the *name* of the proposed corporation, which should not conflict with that of any other Pennsylvania company; second, the *purpose* for which the corporation is to be formed; third, the *place* where its business is to be transacted; fourth, the period of *time* during which it is to exist, which may be perpetual if the organizers so desire; fifth, the *names and residences of the subscribers* and the *number of shares* subscribed by each; sixth, the *number of directors* who are to manage the corporation, with the *names and residences* of those chosen for the first year; and, seventh, the amount of the *authorized capitalization* of the company, together with the *number and par value* of the *shares*, and a statement that *ten per cent of the capital stock has already been paid in cash to the treasurer*, whose name and address should be given.

This application is mailed to the Secretary of the Commonwealth at Harrisburg, along with a check for the bonus drawn to the order of the "State Treasurer," and a second check as a charter fee drawn to the order of the "Secretary of the Commonwealth." The first check should be for one-third of one per cent of the authorized capital. The second check should be for \$30. The authorized capital may be as large as the incorporators desire, but if it is to be over \$1,000,000 some lawyers advise that the company be started with a small capital, which may be *increased* later to the desired amount. The Executive Department—see *Donora Co.* (1903), 27 Pa. C. C. 522—does not now approve charters unless the amount of the author-

ized capital stock is at least \$10,000. The par value of the shares must not exceed \$100, but may be fixed at any sum up to that amount. The application should be confined to the statement of only a single purpose. Many applications are returned for correction where this rule is disregarded. If the business to be incorporated will have a number of branches, such general words should be chosen as to indicate one main, controlling purpose for which the concern is to be organized. If this is phrased in broad terms, a charter can be obtained which authorizes the transaction of numerous kinds of business grouped under one wide purpose. This rule, restricting incorporators to the statement of but one purpose, sometimes drives business men to obtain charters in other states. Applications for the incorporation of manufacturing and mercantile concerns should describe in a general way the character of the goods to be manufactured or sold.

Notice of the intention to apply for a charter should be given by the same *public advertisements* as in the case of corporations of the first class. The notice should give the names of at least three incorporators, designate the time when application will be made to the Governor for the charter, the act of Assembly under which it is made, and the purpose proposed. When the required publication has been completed an affidavit by one of the incorporators should be sent to the Secretary of the Commonwealth, with two copies of the notice attached, as proof of compliance with the statute. Thereupon, if the papers filed are in proper form, the Governor will approve and sign the application certificate, and order letters-patent to be issued. The letters-patent, to which the Governor signs his name, consist of a document prepared at Harrisburg, formally setting forth that the associates are incorporated under the corporate name which they have chosen. The letters-patent are sent to the incorporators, and become the property of the corporation. The original application after having been recorded in the office of the Secretary of the Commonwealth is returned to the incorporators, who should have it recorded also in the office of the Recorder of Deeds for the county where the corporation has its principal place of business. This

application certificate may thenceforth be called the *certificate of incorporation*, because it officially certifies that the state has established the incorporators and their successors as an organized body, on the terms set forth in it.

Thereupon arrangements should be made for a *meeting of the incorporators and other stockholders*. In order to prevent future disputes, a paper should be signed by all of them agreeing upon a certain time and place for the meeting. The meeting should be conducted with proper formality. A chairman and secretary of the meeting should be elected. The certificate of incorporation should be formally accepted and spread on the minutes. Likewise, the letters-patent. The application certificate contains the names of the directors for the first year and of the treasurer, so that there is no necessity for electing these functionaries, unless it is desired to change some of them. The incorporators and other stockholders may elect a president and vice-president, if it is provided that these officers are to be chosen that way. Usually, however, the directors elect the corporate officers. The by-laws and the corporate seal should be adopted, as well as a form of stock certificate. It often happens that the corporation is to issue a quantity of its stock in exchange for a patent, a stock of merchandise, the good will of a business, or other property. The directors and officers of the company should be authorized to carry such arrangements into effect. See the act of April 17, 1876, section 4.

The *by-laws* can usually be made or altered only by the corporate members, and not by the directors. The members of most corporations of the second class, and of some corporations of the first class, are also called stockholders. The word "members" is broader than the word "stockholders," since it may be applied to the associates in all kinds of corporations. The act of May 14, 1891, directs that the by-laws of any corporation created under the act of 1874 shall be its law, subject, however, (1) to the corporate charter, (2) to the act of 1874 and its supplements, (3) to the Pennsylvania Constitution, and (4) to the United States Constitution and statutes. The act of 1891 further provides that the by-laws shall be made by

the members at a general meeting called for that purpose, unless the charter prescribes another body as the makers of the by-laws or a different mode of making them. The by-laws should prescribe the time and place for the members to hold their corporate meetings, the powers and duties of the officials, and such other matters as may be pertinent and necessary for the objects of the corporation. They should give the board of directors power to sell and mortgage real estate, where this authority is to be exercised by the board. They should usually provide for the delegation of certain representative powers to the executive committee and other committees of the board of directors. They may authorize the board to increase or decrease the number of directors without a stockholders' vote on the subject. The by-laws may impose penalties, not exceeding \$20, for the violation of their provisions. See *Bagley v. Oil Co.* (1902), 201 Pa. 78, as to amending the by-laws of a company.

When adopted, the by-laws of a corporation become written into the charter. Parties who deal with the corporate officers should learn the extent of the authority given to these officers by the charter and by-laws: otherwise such parties may find afterwards to their cost that their supposed contract with the corporation is not legally valid. *Cracker Co.'s Estate* (1894), 161 Pa. 157. The members, however, cannot make binding by-laws, if they are unreasonable or in any way contrary to sound public policy. See the case of *Commonwealth v. Benevolent Society*, cited near the beginning of Chapter XXVII.

The directors frequently hold their first meeting after that of the stockholders. They usually proceed at once to elect the president and such other officers as they may find it proper to appoint. The stockholders have exercised their legislative functions in adopting the by-laws. The directors and the officers may be styled the executive functionaries of the corporation, as distinguished from the legislative. The directors pass resolutions selecting some bank or trust company as the depository of the corporate funds, and providing how checks shall be signed. Generally, they take up all matters that may

require immediate attention, including the question of issuing stock for cash or in payment for property purchased by the company.

Promoters who have been instrumental in organizing the corporation, and who want pay for their services, should take care to protect their legal rights. Unless their work has been done at the request of a majority of the other organizers, or the corporation has accepted and utilized the result of their labors, the promoters cannot recover from the corporation even the amounts expended by them in getting the associates together. A promoter should be careful not to incur expenses without having some responsible person agree to reimburse him, unless he is willing to risk losing his money. Where he relies upon getting paid by the corporation after it is formed, he should have a resolution passed by the stockholders or directors to reward him for his services. Any agreement which the incorporators have previously made with him on behalf of the embryo corporation should be formally ratified by the directors at their first meeting, or as soon afterwards as possible.

Those who have made agreements with the organizers of a corporation should remember that the corporation itself is for many purposes an individual in the eye of the law, distinct from the persons who associate to form it. A proposition made to the promoters of a corporation before it is actually formed, and accepted by the promoters and other individual members does not usually bind the corporation. Whoever has made such a proposition should be careful to have it formally accepted by the corporation. The corporation, not having been in existence when the offer was accepted, cannot be bound by the acts of those who assumed to be its agents, unless it subsequently ratifies them. This ratification does not usually need to be formally made, if the company's conduct with reference to the agreement proves an intention to adopt it. It is far safer, however, to have the matter put in proper shape by a definite agreement entered into by the corporation after it is formed. *Tift v. Bank* (1891), 141 Pa. 550.

Promoters who represent that they are acting for a corporation which is to be organized, and that they have bought

property which they will turn over to it at the price paid by them, are bound to display the loyalty which an agent owes his principal. Accordingly, if it is found that they have made a secret profit on the sale of the property to the corporation, they may be compelled to turn this over to the company's treasury. Furthermore, a stockholder who has been deceived by such misrepresentations into subscribing for shares in the company may recover damages from the fraudulent promoters. In ordinary cases, however, there is nothing to prevent the people who organize a company from selling property to it at an advance over the original cost.

CHAPTER XXVI.

THE TERMINATION OF CORPORATIONS.

A corporation, having received a charter from the state, acquires a fixed legal standing. It is an association formally recognized by public authority as intended to bind its members together. The system of membership and government in most corporations is such as to make them more permanent than the ordinary partnership. We studied the termination of agency and of partnerships under five sub-divisions, which will be followed in considering the termination of corporations. The dissolution of a corporation may be caused, first, by agreement; second, by performance; third, by breach; fourth, by impossibility; fifth, by bankruptcy.

(A) Termination of corporations by agreement.

We shall see in the following chapter that a corporation must act in a certain prescribed way. There is not the same authority given to each member as in the case of a partnership, and those who are endowed with authority should exercise it according to corporate regulations.

The act of April 9, 1856, as amended by the act of April 4, 1872, directs that the Court of Common Pleas of the county

where a corporation's principal operations are conducted, or of the county where its principal office or place of business is located, may hear the petition of the corporation, made under the corporate seal, and with the consent of the majority of a meeting of incorporators duly convened, praying for permission to surrender any power contained in its charter, or for the dissolution of such corporation. Notice of the application must be given by publication in two newspapers in the county where the principal operations are conducted and in the county where the principal office is located. The court should be satisfied that the petition may be granted without prejudice to the public welfare or to the members and creditors before making a decree of dissolution. The act of 1856 provides that the surrender of any power by a corporation shall not remove any limitation or restriction in its charter, where the corporation is intended to continue in business. It provides that the accounts of the managers, directors or trustees of any dissolved company shall be settled in the court and approved by it; and that the effects of the company shall be divided among the members entitled thereto, as in the case of the accounts of assignees and trustees. This act does not permit property devoted to religious, literary, or charitable uses to be diverted from the objects to which they were given or granted. The decree of the court, ordering dissolution, does not go into effect until a certified copy thereof is filed and recorded at Harrisburg in the office of the Secretary of the Commonwealth.

This act gives the Courts of Common Pleas jurisdiction not only over corporations of the first class, which they have helped to form, but also over corporations of the second class, which have received their charters from the Governor. The courts will not grant the petition for dissolution unless they feel satisfied that no injustice will be done the stockholders. Ample notice of the meeting at which a vote is to be taken on the question of dissolution should, therefore, be given to all stockholders, and the proceedings at the meeting should be conducted with due formality.

If the corporation to be dissolved is small, and there are but few stockholders, it may save expense to dissolve without

consulting the state authorities. Suppose all the stockholders are of full age and sound mind, and agree unanimously that the corporation shall be considered as at an end. If all its debts are paid, and the members can trust each other not to raise trouble in the future, this course may be adopted. Every single member should sign and seal the agreement of dissolution. This short cut, however, is not to be recommended, because it is usually better to follow established methods of procedure.

(B) Termination of corporations by performance.

Where a corporation is organized for a limited period, it comes to an end at the expiration of that period. The officers should not attempt to transact any more business, but should proceed to wind up the company's affairs. A renewal of the charter may be obtained under the general corporation act of 1874. If it is desired to continue in business, an application should be prepared, containing the same information as in the case of an entirely new company, and should also state the following facts: first, that it is a renewal of the former charter, giving the date of the first charter; second, that a majority in interest of the company consent to the re-chartering, as must appear by a certificate under the corporate seal; third, what the financial condition of the company is, at the date of the application, with respect to capital stock paid in, funded debt, floating debt, estimated value of property and cash assets, if any. Furthermore, there must be an express acceptance of the provisions of the Pennsylvania Constitution and of the corporation act of 1874, and a surrender of all such privileges conferred on the corporation by its original charter as are not enjoyed by corporations of the same class under the act of 1874 or the general laws of Pennsylvania.

The application should be made to the Court of Common Pleas, if the corporation belongs to the first class, and to the Executive Department at Harrisburg if it belongs to the second class. Upon the granting of the application the re-chartered company succeeds to all the rights and liabilities of the old company.

Where a corporation has been expressly chartered to put through a certain piece of work, and the work is completed, there is no further reason for its continuing in existence. If the officers attempt to involve the company in other matters which are clearly outside of the business for which it was formed, the members who object to this departure may obtain the aid of the court in preventing it, and in securing a dissolution of the company.

(C) *'Termination of corporations by breach.*

The mere failure to elect corporate officers at the proper time does not bring about a dissolution. Indeed, very few corporations are dissolved for any omission to comply with the law (apart from the failure to pay taxes) or for the commission of any wrong. The failure to pay taxes leads to the dissolution of many companies by the state. Any corporation of the second class which does not, within two years of the date of its letters patent, proceed in good faith to organize and do the things contemplated in its charter and have at least quarter of its capital paid up, may have its charter forfeited at the instance of the Attorney-General.

The act of March 17, 1853, provides that if any corporation shall misuse or fail to use its franchise, or do anything, whether by way of omission or commission, justifying the forfeiture of its franchise, judicial proceedings may be instituted to annul the company's charter. For instance, such proceedings may be invoked against a turnpike company which is given the right to collect toll in consideration of its agreement to keep a road in repair, and which fails to repair the road. The state rarely interferes with the operations of purely private companies, such as manufacturing companies, which do not exercise semi-public functions, like that of maintaining a railroad or a turnpike. Upon the dissolution of a corporation in such proceedings, a receiver is usually appointed by the court to take charge of the corporate property, and make final distribution. This receiver succeeds to the rights of the dissolved company, and suits should thereafter be brought, and all business transacted in his name as receiver, rather than in

the name of the defunct company itself. More will be said about receiverships towards the end of this chapter.

(D) Termination of corporations by impossibility.

Under Agency and Partnership, we saw that the death of the agent, or of the principal, or of a partner, usually terminates these forms of association. The personal relationship is usually an essential feature, and the death of one of the persons terminates it. In corporations, on the contrary, as we shall see in the next chapter, the personality of the members is a matter of indifference. When a stockholder dies his shares of stock pass automatically to his executor or administrator, unless he has provided otherwise by the terms of a will. You may imagine, however, that all the members of a small corporation might die at the same time in some shipwreck or other big accident, without making a will and without leaving any known heirs. In that case, their property, including their shares of stock, would escheat to the Commonwealth of Pennsylvania, as we shall see in the fifth book. Thereupon, the company would probably be deemed to be dissolved, and the state authorities would have its assets distributed, and the net proceeds paid into the State Treasury.

(E) Termination of corporations by insolvency or bankruptcy.

Mere insolvency or even an assignment for the benefit of its creditors does not effect the dissolution of a corporation. It would seem, however, that a corporation is terminated by a sheriff's sale of all its rights and franchises. When a corporation becomes insolvent, we know from chapter seventeen that it cannot be forced into bankruptcy unless it has committed one of the five acts mentioned by the bankrupt statute of 1898. The corporation itself cannot make a voluntary petition to go into bankruptcy, and the refusal of Congress to let this be done is due, perhaps, to two reasons. First, because the bankrupt act was framed largely to secure a discharge for persons crushed down by debt. Since the corporation itself, as a being distinct from its members, is regarded as owing the corporate debts, and since any possible personal obligations which may

be cast on the members can usually, under appropriate circumstances, be discharged through bankruptcy proceedings, there is no reason for granting a discharge in bankruptcy to the ordinary corporation itself. Second, the state laws provide an adequate system for administering the effects of insolvent companies, and winding them up finally. Certain semi-public corporations, a railroad company, for instance, need to be continued in existence, in spite of insolvency, and special rules are laid down by the courts to suit such cases.

The ordinary individual is considered insolvent when his liabilities exceed his assets, or when his affairs are so tied up that he cannot meet maturing obligations. In the case of a corporation, you have usually no personal liability resting on the members, but as a substitute the law provides that business corporations shall have a certain capital. This is originally fixed when the corporation is first chartered, and may be increased from time to time through appropriate legal proceedings. From a bookkeeping standpoint, a corporation is insolvent when its capital becomes impaired. The capital stock paid in is charged against it to the debit account, and if the assets on hand amount to less than the total liabilities, the corporation shows a balance on the wrong side of the ledger. Proceedings in bankruptcy, however, and also proceedings in the state courts, are usually based, not merely on the latter kind of insolvency, but on something more substantial, as in the case above mentioned of an individual debtor. It was explained at the end of the first book that the national bankruptcy act has largely superseded the control of our state courts over the estates of insolvents. The following remarks apply, however, to such corporations as are not affected by the national act.

When the principal or interest of a corporation mortgage is unpaid at maturity, or when a judgment cannot be satisfied by a sale of any corporate property which is open to seizure, the disappointed creditor may usually file a petition in court for the appointment of a receiver. Sometimes even a creditor who has not obtained judgment may have a receiver appointed for an insolvent corporation which admits the debt, if to obtain

judgment and to send the sheriff to look for corporate property would be only a useless formality. Again, receivers are sometimes appointed at the instance of shareholders or others interested in a company to prevent the property from being sacrificed by forced sales, or to prevent the officers from grossly abusing their trust. The courts, however, will not interfere in the petty domestic squabbles which sometimes arise among the members of a company and those in charge of it. When receivers for solvent corporations are appointed by the Pennsylvania courts, the Federal act of 1898 and the State act of 1901 do not affect the proceedings.

Receivership proceedings do not always point to the termination of a company, for many receivers are put into office merely to tide over some temporary emergency. This has been done in the case of many railroads and other semi-public corporations, the nature of whose business may require them to be kept going in order to prevent a complete sacrifice of the interests of creditors and stockholders. A temporary receiver is often given extensive authority, but when he has discharged his functions, he turns the property over to the corporate officers, so that the company may enjoy a new lease of life. A receiver who is appointed to wind up a corporation should proceed promptly to gather in assets, and arrange for its final dissolution. He should ordinarily enter into no new business on behalf of a corporation which is to be terminated, although in the case of a manufacturing company the Supreme Court has permitted a receiver to work up raw materials in order to get a fair price for them. The receiver may make contracts for the employment of watchmen and other necessary agents and may take all steps required to fulfil the duties of his office. One of his first duties is to see that the property in his hands is insured against fire, where the property is of such a kind as is usually insured. He should get an order of court to sell the corporate property, and the sale should be advertised as subject to the court's confirmation. The sale should ordinarily be at public auction, and if the best bid can be bettered by an advance of ten per cent or over, the court will usually refuse to confirm it, and order a resale.

The case of *Trust Co. v. Railroad Co.* (1899), 189 Pa. 363, shows that the notice of sale should clearly state the terms under which title will be passed to a purchaser. A mortgage was given by the Squirrel Hill Railroad Company to secure certain bonds, on which this suit was brought by the trust company. Five months after the bonds were issued a receiver was appointed for the company, who sold its road and franchises and all other property to a man named Noble. Noble turned them over to the railroad company, which was the defendant in the suit. No notice of the sale before its occurrence had been given to the owner of the bonds or to the trustee under the corporate mortgage, and the only subsequent notice did not mention that the property would be sold clear of the mortgage. Furthermore, there was no reference to the mortgage or to any intention of disturbing existing liens in the petition for the sale, in the order of court authorizing it, or the order confirming it. The court held that the former mortgage was still a lien upon the railroad property. The holder of a mortgage has usually a preferred claim against the property which it covers, and it would be wrong to interfere with his lien, unless the court has ordered that the property shall be sold clear of it. Such an order of court almost always provides that legal notice shall be given to the mortgagees or other lien holders, in order that they may get the benefit of their liens by bidding up the property when it is sold, and thus securing a fund out of which their prior claims may be paid.

When a receiver is appointed for a company which is to be dissolved, the rights of the various claimants against it are fixed as of that date. No creditor may subsequently acquire an advantage over the others by legal proceedings. Even proceedings which have been already started may be set aside where this course will advance the general interest. In the case of *Manufacturing Co. v. Watch Co.* (1894), 161 Pa. 17, it appeared that a creditor of the watch company had entered judgment on the company's bond, and sent the sheriff to sell its property. A few days later, the manufacturing company and other creditors filed a bill in equity against the watch company under which receivers were appointed. The receivers

petitioned for an injunction to prevent the sheriff from selling the property which he had seized, alleging that this would result in a sacrifice. The Supreme Court decided that an injunction ought not to be granted, for the creditor who had obtained judgment was merely pursuing the regular methods for collecting it. No evidence appeared of a fraudulent intent to prefer this creditor, or of any collusion with the debtor. If the 1898 bankrupt act had then been in force, the manufacturing company and the other creditors who wanted to prevent the sheriff's sale would probably have filed a bankruptcy petition, which may be done in involuntary proceedings against corporations engaged principally in manufacturing, trading, printing, publishing, mining or mercantile pursuits. The United States District Court will promptly restrain sheriff's sales of an insolvent debtor's property, if a proper bankruptcy petition is presented by creditors opposed to the sale, under circumstances like those in the case of *Manufacturing Co. v. Watch Co.* The state courts, too, will restrain such sales when opposing creditors take proceedings under the Pennsylvania act of June 4, 1901, in cases where this act may be invoked.

A receiver must not be hampered in the exercise of his duties, and the court will uphold him against the officers of the company who may try to prevent him from learning about the company's affairs. He can compel the delivery to him of the company's books. Besides collecting what is due the company from those who have borrowed money or bought goods from it or incurred any other debts to it, the receiver should also collect any unpaid subscriptions to stock. The receiver of a mutual insurance company should proceed at once to levy an assessment upon the members, in case the members may be legally assessed. In attending to all these matters he should be guided by ordinary business prudence. It is equally wrong for him to waste the moneys of the estate in litigation which does not promise any success or to omit, out of a timid fear of incurring legal costs, to bring a lawsuit which bids fair to increase the assets in his hands. The duties of a receiver were discussed in the case of *Schwartz v. Oil Co.* (1893), 153 Pa. 283. The Supreme Court stated that the

receiver occupies a fiduciary relation to the owners of the property under his care and to all who have claims upon it. He is subject in all things to the control of the court, whose officer he is, and when in doubt about his duty in any particular it is his privilege to apply to the court for specific instruction. He is bound, as a trustee, to exercise prudence and good faith in all his dealings, and to bring to the discharge of his official duties the same measure of skill and the same personal supervision that he would give if the estate were his own.

In the case of *Schwartz v. Oil Co.*, just mentioned, it was stated that a receiver's compensation is not regulated by statute, but must be settled by the court which appointed him and has jurisdiction over his accounts. The amount of his compensation does not depend on his wealth or social standing or the demands made upon his time by private business. The court considers what time and labor were needed to perform his duties, and their fair value as measured by common business standards; also the degree of activity, integrity and dispatch with which his work is conducted. When there is clear proof of delay in closing up his accounts, inattention to his trust, use of trust funds for the receiver's own private business, or a want in any other particular of the good faith and diligence required of him, his compensation may be reduced below the ordinary standard or denied altogether. Allowances for expenses should be carefully scrutinized, and if they are unnecessary or extravagant they should be disallowed altogether or reduced. The same is true of bills for the employment of counsel, and the expenses incident to conducting legal proceedings. In passing upon bills it should be inquired whether or not the receiver would have paid the same salaries to his personal employees, surrounded himself with the same array of professional advisers at the same cost, and adopted the same general line of management, if he had been transacting his own business. If he employs another to do the work which he should undertake himself, he cannot charge the estate with the salary paid to his substitute. The receiver in the case mentioned above had obtained an order of court permitting the loan of the trust

funds to banks. He lent \$58,000 for three years to two banks of his own, at about one per cent interest, and the Supreme Court declared that even the lower court's previous order, permitting the receiver to make these loans, would not shield him from responsibility. He knew the value of money, and so he was surcharged with an additional four per cent for three years on the fund thus converted to his own selfish benefit. The delinquent receiver was allowed \$4,000 as compensation, in spite of several improper actions by him. Three thousand dollars were allowed for his work during the first year, and the remaining \$1,000 for his work during the two other years of his administration.

The Pennsylvania courts have no jurisdiction to appoint a receiver for a corporation of another state, which has not established an office and appointed an agent here, as required by the act of April 22, 1874. This act will be mentioned hereafter. Under any circumstances, the Pennsylvania judges will be slow to appoint a receiver for a company chartered elsewhere, unless satisfied that the interests of Pennsylvanians demand an administration of the corporate affairs under the control of local courts. In the case of *Schmitz v. Condense Co.* (1902), 11 D. R. 442, a receiver was appointed for a Delaware corporation in Philadelphia. All the officers and directors, except one, resided in Philadelphia, and most of the assets were there. It appeared that the treasurer had misappropriated corporate funds, and was preventing, through his control of the board of directors, the institution of a lawsuit against him. The court declared this to be good ground for appointing a receiver. On the other hand, a Pennsylvania court will never interfere with matters of purely internal management of a foreign corporation, as, for instance, the making of an unwise and reckless contract. See the case of *Madden v. Light Co.* (1897), 181 Pa. 617.

Where the courts of another state have appointed a receiver for a corporation chartered in the same state, our courts will not favor the foreign receiver at the expense of Pennsylvanians. In the case of *Frowert v. Blank* (1903), 205 Pa. 299, it was decided that the Pennsylvania holders of

matured death certificates of an insolvent New York beneficial association are entitled to payment out of a fund belonging to the association in Pennsylvania before any part of it is handed over to a New York receiver. This was a fraternal association without capital stock, and it was authorized to insure its members against death and disability. To meet its liabilities, it had power to assess its members, fifteen per cent of whom were Pennsylvanians. Frowert, a Philadelphian, was the "imperial treasurer," and as such had over \$32,000 on deposit in a Philadelphia bank collected from assessments upon all the members of the association. When the New York court appointed a receiver, there were about sixty-five death claimants, fifteen of whom resided in Pennsylvania. Upon a bill in equity filed by Frowert, I. N. Solis was appointed ancillary (that is, auxiliary) receiver of the association in Pennsylvania. Our Supreme Court stated that the New York receiver had no power beyond New York, except where permitted by courtesy to exercise the functions of his office in another state in cases where the rights of domestic creditors will not be infringed. Every state should uphold the claims of its citizens against insolvent parties by retaining within its own jurisdiction and control whatever part of their property may be located in such state, until the rights of its own citizens have been satisfied. This principle is applied where a resident of another state dies leaving property in Pennsylvania, which is claimed by Pennsylvania creditors, as will be seen in the fifth book.

When a receiver has completed his work, he should prepare an account showing completely what he has done, and this account is frequently referred by the court to an auditor. Section 26 of the act of June 4, 1901, given at length in the seventeenth chapter, provides for an auditor only in certain cases, but the practice of some courts is to appoint one anyhow. A reference to the act will show the subsequent proceedings in estates wound up under its provisions.

CHAPTER XXVII.

ADMISSION TO MEMBERSHIP IN A CORPORATION, EXPULSION
THEREFROM AND TRANSFER OF INTERESTS THEREIN.

The word "member" usually means a stockholder in the case of corporations of the second class and generally in all business concerns. Most corporations of the first class do not have a capital stock, and membership in them is largely a matter of personal qualifications. Where a man has stock in a business company, his membership is largely a matter of property rights.

The corporation act of 1874 and other Pennsylvania corporation statutes provide for the formation of concerns which are to last either during a limited term or perpetually, as the organizers may designate in their application certificate. It is obvious that none of the original incorporators of a company will live forever, and, therefore, an important feature of corporations lies in the fact that the ranks of membership may be replenished with outsiders, although the association remains the same. In the case of the ordinary partnership, we saw that ordinarily the death of any member instantly terminates the firm. The special and limited partnerships which gradually approach a corporation in their characteristics provide for the possibility of preserving the firm in spite of death. In a corporation the scheme of management is such that the membership may completely change without disturbing the conduct of the corporate affairs.

(A) Membership in corporations of the first class.

Membership in a corporation of the first class is usually regulated by its charter and by-laws. These are binding unless they violate some provision of the Federal or state constitution and statutes or some principle of public policy. It is entirely proper to impose restrictions on the admission of members to a beneficial, social, literary or religious corporation. Even where a man has been admitted to membership, he may be

expelled when this is necessary in order that the corporate body may be governed in peace. See *Reformed Church v. Commonwealth* (1846), 3 Pa. 282. A member of a religious corporation had been excommunicated for libelling the pastor and other members of the church, and refusing to submit himself to church discipline. The state court held that he should not have brought civil proceedings without appealing from the decree of excommunication to the higher ecclesiastical courts. If these church courts should reverse the decree against him, the member could obtain aid by mandamus proceedings from the civil authorities in case his pastor refused to reinstate him. The Pennsylvania Supreme Court declared that the decisions of ecclesiastical courts are final, for these are the best judges of what constitutes an offense against the word of God and church discipline. Any other courts must be incompetent judges in such matters.

A similar point arose in the case of *Commonwealth v. Benevolent Society* (1810), 2 Binney 440. John Binns had accused William Duane, the president of the society, of certain ungenerous and improper conduct. Duane had Binns expelled, on the ground that the charter of the society gave authority to make by-laws, and that a by-law had been passed subjecting a member to expulsion for vilifying another. The court ordered Binns restored to the rights of membership, for without an express power in the charter nobody can be expelled, unless he has been guilty of some offense, which either affects the interests or good government of the corporation, or is indictable by the law of the land. Expulsion may be necessary in order to preserve order at the meetings of a society, but it is not justified where the only complaint is founded on a private quarrel between members, totally unconnected with the society's affairs.

(B) *Membership in corporations of the second class.*

In corporations of the second class, the relation among the members is not a close personal relation, but largely that of co-owners of a business. The business is so conducted that the personality of any individual stockholder has not much legal

bearing upon his associates. Ownership in corporate stock is a property right, which the courts want to have freely transferable. This applies not only to corporations of the second class under the act of 1874, but also to most concerns chartered under other acts. In the case of *Commonwealth v. Detwiller* (1890), 131 Pa. 614, an attempt was made to deprive a citizen of New Jersey of the right to vote stock in the Farmers' and Mechanics' Institute, chartered under an old Pennsylvania act, and of the right to become a director of the institute. The Supreme Court held that the right to buy, hold, use and enjoy personal property, whether corporate stock or articles of merchandise is not dependent upon citizenship, and that even a subject of some foreign monarch may possess it. The office of a corporate director is not a political one, and a foreigner, whose nation is not at war with the United States, may become a director of any company when not expressly made ineligible by the charter. Since he can acquire the stock, he can acquire it with all the rights and privileges which its ownership confers, among which is the right to have a voice in the control of its affairs.

The courts are so desirous to have corporation stock transferable that in *White v. Ryan* (1894), 15 Pa. C. C. 170, the agreement of some stockholders not to dispose of their stock without the consent of all the parties to the agreement was held to be not enforceable, even though the party who broke the agreement was about to transfer his stock to a foreign corporation. It made no difference that the foreign corporation was thus acquiring a controlling majority of the Pennsylvania company's stock. Again, in *Vanderbilt v. Bennett* (1887), 6 Pa. C. C. 193, a voting trust was declared illegal. Some stockholders of a railroad company had transferred their stock to trustees, so that the trustees might control the policy of the road. The stockholders retained the right to receive dividends, and all the incidents of ownership except the power to vote. One of the stockholders afterwards obtained an injunction to prevent the trustees from voting his shares. Even if such an arrangement were allowable at all, it would seem to give the trustees nothing more than a proxy to vote the stock trans-

ferred to them, which any of the real owners could revoke at his pleasure.

There has been no Pennsylvania Supreme Court decision on this subject, and the two cases just mentioned should be read in connection with the case of *Shelmerdine v. Welsh* (1890), 20 Phila. 199. In this case a voting trust had been formed by a majority of the creditors and stockholders of an insolvent railroad company, in order to reorganize the concern, and afterwards elect a president and managers. The holder of 1,000 shares of stock asked for an injunction to restrain the voting trustees from electing their ticket, but the Court of Common Pleas refused to grant it. The trustees' authority to vote the stock was *coupled with an interest*, for they represented the *creditors* as well as stockholders, and were endeavoring in the interests of all parties to re-establish the company on a sound basis. The coupling of a power with an interest is treated in Chapter XIX, subdivision (C). See also *Morgan v. Gas Co.* (1904), 30 Pa. C. C. 22.

In the case of *Rigg v. Railway Co.* (1899), 191 Pa. 298, the Supreme Court approved of an agreement among certain stockholders to stand together in carrying out an honest business policy, consistent with what they believed to be the best interests of all the stockholders. This does not justify a pooling agreement for vesting the government of the corporation in certain members of it, or for yielding the control to a few, who might dominate regardless of the interests of the many. In this case the Supreme Court hints that usually voting trusts are not legal. In the case of *Fitzsimmons v. Lindsay* (1903), 205 Pa. 79, the court upheld an agreement among all the shareholders of a hardware company that on the death of any of the parties thereto, the remaining stockholders should have an option to buy the decedent's stock at its book value. For further legal proceedings upon this agreement, read *Lindsay's Estate* (1904), 210 Pa. 224.

The act of June 24, 1895, amending the corporation act of 1874, provides that any *stockholder of a corporation shall be entitled to receive a certificate of the number of shares* standing to his, her or their credit on the books of the corporation, signed

by the president or vice president or other officer designated by the board of directors, countersigned by the treasurer, and sealed with the corporate seal, which certificate shall be transferable at the holder's pleasure, either in person or by his agent duly authorized as the by-laws may prescribe. This act provides that any transfer shall be made subject to all payments due or to become due on the stock, and that the assignee or party to whom the same shall have been transferred shall be a member of said corporation, and enjoy all the immunities, privileges and franchises, and be subject to all the liabilities, conditions and penalties incident thereto, in the same manner as the original subscriber or holder would have been. Upon a sale of such stock in satisfaction of any debt for which it is pledged, the purchaser shall have the right to compel a transfer of such stock upon the corporation books and the delivery of a proper certificate therefor. The stock of every corporation created under the act of April 29, 1874, and its supplements, is regarded as personal property; and no share shall be transferable until all previous calls thereon shall have been fully paid in, or shall have been declared forfeited for the non-payment of calls thereon. No note or obligation given by a stockholder, whether secured by pledge or otherwise, shall be considered as payment of any part of the capital stock.

The Constitution of Pennsylvania prohibits any county, city, borough, township or incorporated district from becoming a stockholder in any company, association or corporation, and from obtaining or appropriating money for and from loaning its credit to any corporation, association, institution or individual. The Constitution also prevents the state itself from becoming a joint owner or stockholder in any company or association or corporation. The act of July 2, 1901, allows all corporations organized for profit to purchase, hold, sell, assign, transfer, pledge or otherwise dispose of shares of the capital stock, or of any bonds, securities or evidences of indebtedness of any other corporation or corporations of this or any other state. A Pennsylvania corporation, while the owner of another company's stock, may exercise all the rights, powers and privileges of ownership, including the right to vote thereon. The

Supreme Court stated in the case of *Coleman v. Oil Co.* (1865), 51 Pa. 74, that the employment of corporate funds to speculate in the stock of the same corporation is not a practice to be encouraged. In that case, and also in the case of *Dock v. Cordage Co.* (1895), 167 Pa. 370, it appeared that a corporation had bought its own stock, and afterwards distributed the stock among its shareholders, but neither transaction was set aside. It would seem, therefore, that such a purchase will be upheld, unless proved to be specially harmful to some of those interested in the corporation.

(C) *Powers of attorney to transfer stock.*

In the eighteenth chapter the subject of agency by estoppel was dealt with, and we saw that where a man clothes another with the appearance of being his agent, he cannot deny the seeming authority as against an innocent third party whom he has helped to mislead. Apply this to a question which often arises regarding the transfer of corporation stock. Does a stockholder constitute another his agent to transfer corporation stock by handing him the stock certificate? Suppose that a certificate for ten shares of Pennsylvania Railroad Company stock made out in John Smith's name, which Smith has left with his broker, Henry Pole, for safe keeping, is handed by Pole to an innocent third party. The latter does not acquire a good title to the stock, by the mere delivery of the certificate to him, even though he pays its value to Smith's broker, who embezzles the proceeds. Suppose, however, that Smith signs a power of attorney according to the following customary form:

KNOW ALL MEN BY THESE PRESENTS, *THAT*.....
 for value received, have bargained, sold, assigned, and transferred, and
 by these presents do bargain, sell, assign and transfer unto.....
shares of thestock of the standing
 in name on the books of the, and do hereby consti-
 tute and appoint true and lawful attorney, irrevocable,
 for and in name and stead, but to use,
 to sell, assign, transfer and set over all or any part of the said stock,
 and for that purpose to make and execute all necessary acts of assign-
 ment and transfer, and one or more persons to substitute with like full

power, hereby ratifying and confirming all that said attorney, or substitute or substitutes shall lawfully do by virtue hereof.

IN WITNESS WHEREOF, have hereunto set.....
hand and seal theday of, 190....

Sealed and delivered in
the presence of

..... [L. s.]

A form somewhat like the foregoing is usually printed on the back of a stock certificate, but it is preferable to sign a detached power of attorney, unless the transfer is to be made at once. Now suppose that Pole, whom Smith has told to hold the stock certificate, fraudulently takes advantage of the power of attorney, and sells or pledges the stock to an innocent third party. The latter would have a perfect right to retain the stock as against Smith, even though he learned of the fraud before the stock was actually transferred out of Smith's name on the books of the corporation, provided that he parted with value for the stock before hearing of Pole's fraud. By commercial usage, a stock certificate coupled with a signed, irrevocable power of attorney, either filled up or blank, is, in the hands of a third party, presumptive evidence of ownership in the holder. This principle was thoroughly expounded in the case of *Shattuck v. Cement Co.* (1903), 205 Pa. 197. See also the case of *Wadlinger v. Bank* (1904), 209 Pa. 197.

A creditor of John Smith could not attach Smith's interest in the company after the third party had given value for the stock certificate, accompanied with a blank power of attorney. You can see, therefore, that one's interest in a stock corporation is to a certain extent represented by one's certificate of stock. Stock often passes through a number of hands, without any record of the successive transfers upon the corporation books. Sometimes the owner will pledge it with a bank for a loan, delivering the certificate and a blank power of attorney, and the bank will return these papers to him upon the repayment of the loan, without having used the power of attorney to secure a transfer of the stock on the corporate books. Then the same owner may get another loan and give the same pledge at another bank, and after repaying this second loan, he may

use the same papers to transfer the ownership of the stock to a purchaser. It is wise for a banker or other person who lends money on collateral to have the contract fully expressed in writing, and the following form of agreement is recommended as covering a number of legal points. Suppose a man is borrowing some money from the Market Street National Bank, and is pledging certain collateral. The following form is applicable to the pledging of stocks, bonds and many other kinds of collateral:'

PHILADELPHIA,190....
 \$.....
 On demandpromise to pay to the order of

DOLLARS,
 with interest from date, WITHOUT DEFALCATION, FOR VALUE RECEIVED;
 and have delivered, as collateral security

and do agree, on demand, to deposit with the holders such additional security as they may from time to time require; and in default thereof, this note shall instantly become due and payable as though it had actually matured; and upon default of payment at maturity, whether such maturity occurs by expiration of time or default in depositing additional security as above agreed, do hereby authorize and empower the holders hereof, for the purpose of liquidation of this note and of all interests and costs thereon, to sell, transfer and deliver the whole or any part of such security, or any additions thereto, or substitute therefor, without any previous demand, advertisement or notice, either at brokers' board or public or private sale, at any time or times thereafter, with the right on the part of such holder to become the purchaser and absolute owner thereof, free of all trusts and claims. And it is further agreed, that the securities hereby pledged, together with any that may be pledged hereafter, shall be applicable in like manner to secure the payment of any past or of any future obligations of the undersigned held by the holders of this obligation; and all such securities in their hands shall stand as one general continuing collateral security for the whole of said obligations, so that the deficiency on any one shall be made good from the collaterals for the rest; hereby remaining responsible for any deficiency in payment, and waiving any benefit, exemption or privilege under any law now or hereafter to be in force.

PAYABLE AT
 THE MARKET STREET NATIONAL BANK.

.....
 Although a shareholder, who puts his stock certificate with a power of attorney in the hands of another, clothes the latter with the apparent authority of an agent, he may, of course, instruct the agent not to exercise this authority. If the agent disobeys this instruction, a third person who buys the stock from the agent with knowledge of the latter's disobedience has no rights as against the principal. If the principal acts promptly, he may, perhaps, prevent the third party from transferring the stock to an innocent fourth party. So long as the

stock remains in the possession of the third party who participated in the agent's fraud, the principal may repudiate what his agent did, for the doctrine of estoppel cannot be invoked against him. These rules were touched on in the chapters about agency.

If a broker or other agent fraudulently abuses a power of attorney placed in his hands, he is answerable to his principal, not only in a civil action for damages, but also criminally. Even if a party who lends money on collateral merely repledges the security without the borrower's consent, he commits a crime under the act of June 10, 1881. This act does not, however, prevent brokers from pledging stocks or other securities which they have purchased, wholly or partly, with their own money or credit, for others, and for which they have not been fully reimbursed by those for whom such stocks or securities have been purchased.

(D) *Fraudulent issue of stock by corporate officers.*

We have been considering transfers of stock mainly with reference to the rights of a purchaser or pledgee as against the former owner. Let us see what are his rights as against the corporation which issued the stock. In *Kisterbock's Appeal* (1889), 127 Pa. 601, it appeared that Kisterbock had advanced money upon certificates for 300 shares of stock of a street railway company, which had been fraudulently issued by the corporate officers. The Supreme Court held that his only right as against the corporation was to recover the amount of his loan, with interest. He could not demand that the certificate be regarded as genuine. He could only claim from the corporation reimbursement of the sums advanced by him to the holder of the certificates who pledged them to him. In the case of *Commonwealth v. Traction Co.* (1902), 204 Pa. 151, a company filed a bill in equity to have an issue of its capital stock annulled, on the ground that it was practically without consideration and fictitious. The bankers who profited by this issue had sold the stock to third persons before the bill was filed. The company had delayed some years in asserting its rights, and the court dismissed its bill because of this delay

and of the fact that innocent third persons had subsequently bought the stock.

In *Wright's Appeal* (1882), 99 Pa. 425, a holder of stock which had been fraudulently issued to her was refused any legal relief against the corporation. John S. Morton, the president of the company, the same company that figured in *Kisterbock's Appeal*, was Ellen E. Wright's nephew. She delivered to him certificates for 1,780 shares of the capital stock, taking his individual due bills for them. She executed powers of attorney, in order that he might borrow money on them, which he said was needed by the company. Morton pledged a number of Wright's certificates, and under the powers of attorney which she had given 1,380 shares were wrongfully sold and transferred to parties who were holders for value and without notice of the fraud. Wright received dividends, sometimes from the company and sometimes by individual checks which Morton gave her to hide his appropriation of the stock. When she asked him to return what she had loaned, he gave her other certificates of stock signed by the proper officers of the company, who were in conspiracy with him, and attested by the corporate seal. These new certificates were issued in excess of the capital limited by the charter of the company, which received no value for them. After some years Morton was exposed, and litigation ensued between Wright and the company. Wright contended that the corporation was liable for its president's actions. Morton had been given full charge of the corporate affairs, but he had never been authorized to borrow stock certificates on behalf of the company. Neither was there evidence that he had ever been authorized to borrow money for the company, and none of the money which he had raised from Wright's stock had gone into the corporate treasury. The court held that Wright could not throw the consequences of her misplaced confidence upon the corporation, for Morton had not been its agent in his dealings with her. The implied powers of the president of a company, like those of any other agent, must be considered in connection with the usual and legitimate business of the principal. Had Morton contracted on behalf of the company for the lease of an office,

or the purchase of horses, cars or materials needed in its business, he would have bound the company. He could not bind it, when borrowing upon his own due bill with the intention of using the money for himself, merely by falsely representing that he wanted the money for the corporation.

Compare the case of *Cooke v. Marshall* (1899), 191 Pa. 315, where no question of fraud was presented. It appeared that a corporation had issued stock, although chartered under an act which did not give it authority to do so. The court held that any issue, increase or reduction of stock not authorized by law is void. After a re-argument, however, the court suggested that upon a reorganization of the concern, the proportionate interests of the several parties holding stock might, perhaps, be recognized as the basis upon which to found the final division of interests in the corporation. *Cooke v. Marshall* (1900), 196 Pa. 200. The Constitution of Pennsylvania directs that "no corporation shall issue stocks or bonds except for money, labor done, or money or property actually received; and all fictitious increase of stock or indebtedness shall be void." See *Shannon v. Stevenson* (1896), 173 Pa. 419.

(E) *Practical rules about stock certificates for the guidance of stockholders.*

The party to whom a stock certificate is transferred should see that the power of attorney is properly signed by the person in whose name it stands. If the signature does not exactly correspond with the name of the registered owner, the corporate officers may in most cases properly refuse to recognize it. Sometimes the by-laws of a company prescribe that all powers of attorney for the transfer of its shares and of the bonds issued by it must be made on certain printed forms furnished by the company. This is a reasonable regulation, and will be upheld. Where the registered owner dies or becomes insane, corporations properly refuse to allow anybody to transfer the stock, except an executor, administrator or committee duly appointed according to law. If an executor, for instance, wants to transfer stock standing in the name of the decedent, he obtains what is called a "short certificate" from the Register

of Wills before whom he qualified. This short certificate, which costs only a trifle, is filed with the transfer department of the corporation as evidence that the person who transferred the decedent's stock was his legally constituted executor.

If you buy stock, you should have it put in your name at once, unless you intend to sell it again immediately, or unless the financial weakness of the company or some similar reason prompts you to keep your name off its books. The new certificate should be made out in your full name. In this way all your securities will be in exactly the same name. It sometimes causes trouble if you have some stock in your full name and other stock registered with your first initials and only your last name spelled out in full. This advice applies also to registered bonds, deeds, mortgages, bank accounts, credit accounts at stores, and everything else in which the identity of your name may cause confusion. Even your will should be made out and signed with the same name that you use in all business and legal transactions. In addition to seeing that the transfer office of the corporation gets your correct name, you should give your full address. You should also give prompt notice of changes in your address, so that dividends and notices may come to you at once. You should keep an account of the number of shares represented by each certificate, its serial number, the par value of each share, and how much has been paid in on each. Also, whether it represents common or preferred stock, or any special issue. You should enter what you have paid for it. If it is pledged for a loan, the particulars should be set forth. All the dividends received on it should be entered, and you should have a memorandum of the company's dividend rate. The same suggestions are applicable for the most part to corporate bonds.

Unregistered corporate bonds differ from stock certificates in this, that they usually pass by delivery. It is not necessary to have a power of attorney in order to transfer title to most unregistered bonds. Hence, the owner should be particularly careful about keeping them safe. It is regarded as a bad practice for trustees and other confidential agents to invest trust funds in such bonds. All corporate and other securities should,

if possible, be kept in a safe deposit box in the vaults of some responsible bank or trust company. If you carelessly leave an unregistered bond, or a stock certificate with an accompanying power of attorney, where another person can get hold of it, you may be subjected to loss.

If you lend money to a corporation, and take its bond, you become its creditor. The bond is only the paper evidence of the contractual relation between you and the corporation. Likewise, if you own shares of a corporation, you are one of its members and proprietors. Your stock certificate is merely evidence of your relation towards it. Nevertheless, commercial usage enables negotiable bonds, and stock certificates with accompanying powers of attorney, to circulate very much like promissory notes and the other instruments which were discussed in the tenth chapter. Even a thief may pass title to negotiable corporate bonds if he transfers them in the ordinary course of business to a *bona fide* purchaser: *Cochran v. Bank* (1904), 209 Pa. 34. The coupons on such bonds are usually negotiable, and may be detached and negotiated without the bond. These coupons are regarded as distinct promises by the corporation to pay their face value at their respective dates of maturity. If a coupon is refused payment when it falls due it bears interest, although this really involves the compounding of the interest on the bond. The courts are usually opposed to allowing compound interest, and such interest is rarely permitted on any but coupon bonds.

In the tenth chapter it was mentioned that upon the destruction of a negotiable warehouse receipt, certain proceedings in court are required before the goods represented by it can be released from the warehouse. When a stock certificate is lost or destroyed, the owner may have a new one issued to him upon proof by affidavit of the facts. In order to protect the corporation from possibility of fraud or mistake, the owner is required to give a bond with security, so that if the old certificate ever turns up no harm may befall the company.

CHAPTER XXVIII.

THE RIGHT OF STOCKHOLDERS AND OTHER MEMBERS OF CORPORATIONS TO A SHARE OF PROFITS.

A partner is usually both a co-proprietor of the firm and its general agent. A member of a corporation is usually regarded as one of its proprietors, but his right to manage it is quite restricted. The organization of a corporation is such that most of the powers of control are committed by the members to their chosen officers. We shall begin studying the rights of corporate members by seeing what personal benefit they get out of the concern as co-proprietors. Afterwards we shall inquire about their rights of inspection and control.

In many corporations not for profit the benefits and privileges enjoyed by members may be learned from the constitution and by-laws. Most corporations of this class are formed for the mutual advantage of their members, while some of them are purely charitable and intended solely for the benefit of outsiders. The courts are not disposed to interfere with the domestic management of these concerns, for members are expected to conform to the requirements of the charter and of all reasonable by-laws and regulations. A member may, however, obtain judicial relief where his rights have been clearly invaded.

(A) A stockholder's right to dividends.

Coming to the subject of corporations for profit, we may note that the main thing a member of such a corporation generally looks to is the right which he enjoys as one of the owners to a share in the company's earnings. The directors of a corporation should not pay a dividend to stockholders while the corporate capital is impaired. This is a fund which the creditors and others interested in the concern have a right to expect will be kept intact, as far as the uncertainties of business will allow. Even when the capital is unimpaired, the directors have

discretionary power to determine not only the amount of all dividends, including dividends on preferred stock, but also the circumstances under which they may declare them. They are not justified in refusing to declare them either arbitrarily or when, in view of all the circumstances, they ought to grant them. Their action in declaring or refusing to declare a dividend is subject to review by the court, at the instance of a dissatisfied stockholder, but the court will sustain the directors, unless they are clearly abusing their discretion. In the case of *McKean v. Phila. Contributionship* (1897), 181 Pa. 361, it appeared that a mutual insurance company had assets valued at over \$4,000,000, although the whole amount of deposit money or premiums in its possession was less than \$500,000. The amount of insurance outstanding was \$14,573,908. The directors declared a ten per cent dividend, to which McKean, a member of the concern, objected. The court held that one of the inherent rights of trading corporations is to divide their gains among their members. While the Philadelphia Contributionship was formed to protect house owners from loss by fire, there was no reason to prevent the declaration of a dividend out of the accumulated profits. Needless to say, no scheme for returning the deposit moneys in order to secure the whole surplus for a few who might be permitted to remain would be sanctioned by the courts. McKean argued that the company might become involved subsequently in heavy losses from risks assumed by it, but the court answered that this could be urged against the payment of dividends by any banking, transportation, manufacturing or other kind of corporation.

We have seen that a common or preferred shareholder is bound ordinarily to respect the directors' discretion in refusing to declare a dividend. As soon, however, as the directors declare one, for payment at a future date, every stockholder has a right to demand it when the time fixed arrives. The directors usually have no right to revoke what they have done, as appears from *Trust Co.'s Appeal* (1889), 24 W. N. C. 137. A stockholder may bring suit to obtain a declared dividend as soon as it is payable.

(B) *The rights of preferred stockholders.*

Some investors mistakenly fancy that *preferred stock* is like a bond. A holder of corporate bonds is a creditor of the concern, while a preferred stockholder is merely one of the associates who has some rights prior to those of common stockholders. In the case of *Railroad Co. v. Allegheny* (1875), 79 Pa. 210, it appeared that the County of Allegheny had (before the passage of the law which now forbids such transactions) subscribed for certain railroad stock. County bonds were exchanged for the stock, and the railroad company agreed to pay six per cent interest for thirty-two years, *upon the amount of stock so subscribed*, to holders of the bonds in payment of interest thereon. When the company was sued for unpaid interest, its defense was that dividends cannot be declared so as to impair capital stock. A company must conduct its business with money subscribed for its stock. If the money so raised must first go to the payment of interest to the subscribers, the members of a corporation may consume it themselves, and thus impair the rights of creditors. The county was not allowed to stand on a higher level than its fellow-shareholders, and could not ask compensation for its subscription except out of profits.

Sometimes preferred stockholders are entitled only to a priority in the payment of *dividends*. Sometimes they are entitled also to priority in the distribution of *principal* when the company is dissolved. Their rights depend upon the agreement under which their stock was issued. This agreement, while giving them certain priorities, may at the same time put them in other respects at a disadvantage as compared with the common stockholders. The act of 1874 allows every corporation created under it, or accepting its provisions, to issue preferred stock, calling for such dividends as the directors may prescribe, payable only out of net earnings. The consent of a majority in interest of the stockholders must be obtained at a meeting to be called for that purpose, of which public notice must be given during thirty days in a newspaper of the proper county. When preferred stock is issued, it should be decided

whether to make it *cumulative* or not. Holders of cumulative stock, who are not paid dividends on it for a time are entitled to receive dividends for the years when the company paid them nothing, before the common stockholders can begin to share in profits. If a holder of a preferred cumulative six per cent share of the par value of \$100 is paid no dividend during the first year after it is issued, the company must pay him \$12 at the end of the second year before the common stockholders can get anything.

(C) *The right to a dividend, as between various claimants.*

Ordinarily, that party is entitled to dividends in whose name the stock stands at the time it is payable. The directors of a company usually declare a dividend some weeks before the time of payment, and order that it shall be paid to the stockholders of record at the latter date. The corporate books are often closed for about a week prior to the day of payment, in order that a proper list of the stockholders entitled to the dividend may be completed.

Where stock has been pledged, but not transferred to the pledgee's name, the company goes on paying dividends to the registered owner. Where, however, stock held as collateral stands in the pledgee's name, he is entitled to the dividends, as appears from the case of *Boyd v. Worsted Mills* (1892), 149 Pa. 363. Where such dividends have been paid to the former owner who pledged the stock, without the pledgee's consent, the latter may sue the corporation for the amount of the dividends, and the corporation will thus have to pay them twice.

A holder of stock at the time when profits are distributed in the shape of a dividend is usually entitled to them, as against a former holder during the period when they were earned. In the case of *Coleman v. Oil Co.* (1865), 51 Pa. 74, Coleman claimed the benefit of a stock dividend on 500 shares which he had sold before the dividend was declared. While he was the owner of these shares, the company had bought certain shares of its own stock from another party. These were distributed proportionately among the stockholders some months

after Coleman had parted with the 500 shares, and the court held that he must let the purchaser enjoy the benefit of his bargain. This benefit included not only the 500 shares themselves, but also the incidental right to participate in the distribution of the stock dividend.

A different result is sometimes reached by the courts in disputes between beneficiaries of a trust estate. The ordinary holder of stock is absolutely entitled to all that comes out of it, but the situation is somewhat altered where a beneficiary is intended only to derive the income from stock. In *Vinton's Appeal* (1882), 99 Pa. 434, a certain dividend was held to be a distribution, not of income, but of capital. James Martin put 100 shares of the St. Louis Gas Light Company in trust "to receive all issues, dividends and profits accruing therefrom, and to pay over the same to Sarah Vinton during her life, and at her death to transfer said stock to Frederick Vinton, or his legal representatives." Later, the gas light company transferred to a rival concern certain rights and considerable property, receiving in return \$650,000. The directors distributed \$600,000 to the stockholders in the shape of a dividend. Sarah Vinton claimed the entire dividend on the shares held in trust. The court held, however, that the dividend should go to swell the principal of the trust estate, for it was derived, not from *annual earnings or accumulations*, but from *a sale of part of the company's franchises and permanent property*. Those who want to pursue this subject further may read the case of *City of Allegheny v. R. R. Co.* (1897), 179 Pa. 414; also *Smith's Estate* (1891), 140 Pa. 344, and *Oliver's Estate* (1890), 136 Pa. 43. In *Eisner's Estate* (1896), 175 Pa. 143, a similar question arose regarding the right to subscribe at par for 141 new shares in a company whose stock was selling for much above par. The right was worth many thousands of dollars, and the court decided that it must be treated as capital, and added to the body of the trust fund. The rule is the same whether the trustee subscribes for the new stock on behalf of the estate, or sells the right to subscribe for a valuable consideration. See also the case of *Commonwealth v. Transportation Co.* (1891), 145 Pa. 89.

(D) *A stockholder's right to subscribe for new stock.*

Akin to a stockholder's right to his proportionate share of dividends, when declared by the directors, is the right to subscribe for a proportionate amount of a new issue of stock. He may demand such a proportion of the new stock as the number of shares already owned by him bears to the whole number of shares in existence before the increase. See the case of *Electric Co. of America v. Illuminating Co.* (1901), 200 Pa. 516. The Electric Company of America owned 2,283 shares out of a total of 3,994 issued by the Illuminating Company. The directors of the latter concern resolved to sell 650 shares of the unissued capital stock, and to invite sealed bids for the new stock, which was to be awarded to the highest bidder. This scheme would have deprived the Electric Company of America of a majority, had the opposing interests secured the entire new issue. The court granted an injunction to restrain the directors from carrying out their plan. It would be unfair to compel the majority stockholders to make the highest bid for the new stock, in order to retain their control. They would have had to guess the highest price that the minority stockholders, or anyone else, might be willing to pay, and then to bid a trifle over such highest price. The minority stockholders might be very willing to pay a fictitious price, in the sense of a price not warranted by the company's earning power, but founded rather on a desire to get control of it.

CHAPTER XXIX.

THE RIGHTS OF STOCKHOLDERS AND OTHER MEMBERS OF CORPORATIONS TO CONTROL AND INSPECT CORPORATE AFFAIRS.

The members of corporations do not possess, merely as members, the same full powers of management as are enjoyed by the members of a partnership. Most powers of control are lodged in the board of directors and the officers. Even where all the stockholders are individually in favor of a certain

measure, the corporation cannot be said to have adopted it until the proper corporate machinery has been fully operated to accomplish the desired purpose. The case of *Bridge Co. v. Traction Co.* (1900), 196 Pa. 25, stands for the principle that the property of a corporation must be kept distinct from the property of its members, as a separate fund. The City of Pittsburgh had bought the entire stock of the bridge company, but the court held that it did not thereby become the owner of the corporate property, or become entitled to manage or control it. The shares of a corporation constitute a species of property entirely distinct from the corporate property. A shareholder has no private and individual title to the moneys or property of the corporation, nor any actual control over it. Contracts respecting it must be made only by those that have been formally authorized to act on behalf of the corporation. The shares confer mainly a right to participate in profits. All the shares may be held by a single person, and yet the corporation continues to exist; and if the charter or by-laws should require certain acts to be done by more than one stockholder, the sole owner may transfer a portion of his shares to other persons, in order to conform to the letter of the rule. The City of Pittsburgh became a stockholder in the corporation, with rights and privileges as such and nothing more or less. See *Rhawn v. Furnace Co.* (1902), 201 Pa. 637.

Where a party is purchasing a controlling interest in a corporation, it is well to bear this rule in mind. If the board of directors have just been chosen for the following year, they will be entitled to remain in office, despite the changed ownership of the stock, and even though the directors themselves have parted with their own shares. To avoid this, a purchaser of a majority interest will sometimes get those who are selling out to him to arrange for the resignation of several directors in order to give him immediate control of the board. A stockholder or other member of any corporation ordinarily delegates to representatives the power and control of management. His first right in this respect is, therefore, the right to vote for such representatives. In the second place, he has a right to prevent those in charge of the company from grossly abusing their

position. In the third place, he has a right to be consulted in certain extraordinary matters which have not been left to the discretion of his representatives. We shall consider these rights in the order named, appending to the consideration of the first right some remarks about the conduct of corporate meetings.

(A) *The right of a member to vote at the election of corporate directors.*

In the twenty-seventh chapter something was said about a corporate member's voting power and about voting trusts. In corporations of the first class members are often denied the right to vote, and the selection of directors, managers or trustees is vested in some special person or committee. In the case of *Philadelphia Savings Institution* (1836), 1 Wharton 461, the court drew a distinction between religious, charitable, literary and similar corporations, on the one hand, and corporations for profit, on the other hand. In the latter, a pecuniary interest is the evidence of membership; the mere owning of shares gives a right to vote, and a stockholder ceases to be a member by a transfer of his stock.

In almost all corporations for profit each stockholder has one vote for every share. When nothing appears to the contrary in the charter of such a corporation, it is taken for granted that this custom will be observed. Even should the charter or any original agreement among the incorporators of the company attempt to vary this rule, notice of it should be conspicuously printed on the stock certificates, so as to bring it to the attention of all purchasers. The act of May 26, 1893, directs that the stock certificate and transfer books, or either, of any Pennsylvania corporation, shall be evidence of the right of a person named therein to vote thereon as the owner, either personally or by proper proxy. If, however, objection is taken by an actual stockholder at the time the ballot is tendered, accompanied by a written statement under oath that the person in whose name such stock stands on such certificate, or transfer books, and who is offering to vote thereon either in person or by proxy, is not the owner thereof (either in his own right

or as active trustee with the character of his trusteeship disclosed on the face of said certificate or transfer books in connection with his name) it shall be the duty of the judges of election to inquire and determine summarily whether the facts are as reported in such statement, and if so the vote shall be rejected. Where the person named in the certificate or transfer books is not permitted to vote, the real owner of such stock shall have the right to vote on it after furnishing to the election judges satisfactory evidence of ownership.

The act of March 16, 1905, provides that executors, administrators, guardians and trustees, created by a will or by decree of the proper court, shall have the same right, either in person or by proxy, at all corporate meetings, to vote any and all shares of stock held by them in such fiduciary capacity, in any corporation in Pennsylvania or organized under its laws, as the deceased, or legal owner thereof, had in his lifetime, or during his legal ownership thereof. Where there are more than two such *executors, administrators, guardians or trustees*, and a dispute arises among them, the stock shall be voted as the majority may desire. Where stock stands in the name of, say, three persons, who are *co-owners* in their own right, the foregoing act of March 16, 1905, does not apply, and, it would seem, that in the event of a dispute, the stock could not be voted on at all.

The act of May 26, 1893, determines in certain cases the right to vote stock which has been pledged by the owner. It directs that as between the one who pledges the stock and the pledgee, where the pledge is to secure a specific loan with a fixed period or periods of maturity, the right to vote shall be determined as follows: first, by the written agreement of the pledgor and pledgee; second, in all other instances, the pledgor, that is, the party who made the pledge, shall be regarded as the owner and entitled to the right to vote.

Suppose the minority faction of a corporation owns forty-nine per cent of its stock. In order to prevent the majority faction, in a case like this, from denying the other side any representation, the act of April 25, 1876, allows *cumulative* voting. It provides that in all elections for directors, managers or

trustees of any corporation created under the act of 1874, or accepting its provisions, each member or stockholder or other person having a right to vote, may cast all his votes for one candidate, or distribute them upon two or more candidates as he may prefer. Thus, a person who is entitled to one vote for each of six directors, may give a single vote to each of six different directors, or six votes for any one of them, or a less number of votes for any less number of directors, as he may prefer to distribute them. See the State Constitution, Art. XVI.

The statute of March 5, 1903, directs that stockholders of all corporations of Pennsylvania, wherever residing, who shall be entitled to vote at any corporate meeting or election thereof, shall have the right to vote by *proxy* duly executed by the stockholder, either with or without notarial seal or acknowledgment, but properly attested by the signature of a witness. One person may act as proxy for any number of stockholders. Proxies dated more than two months prior to any such meeting or election shall not confer the right to vote thereat. A stockholder who executes a proxy should see that it corresponds exactly with the name appearing on the certificates. Thus if John T. Smith has a stock certificate in that name for ten shares, and another stock certificate for ten shares in the name of John Thomas Smith, he should execute two proxies. A proxy is usually regarded as revocable at the pleasure of the stockholder who gave it. Read in this connection what was said in the twenty-seventh chapter about voting trusts.

The act of May 9, 1889, provides that no stockholder shall be entitled to vote at any meeting or election, on whose share or shares any instalments or arrearages may have been due and unpaid for the period of thirty days immediately preceding such meeting or election.

(B) *The manner of conducting meetings of corporate members.*

Meetings of corporate members should be held in *Pennsylvania* at the company's *principal office*, formally designated as such in the company's yearly report which is mentioned in Chapter XXXIV. See *Council v. Council* (1900), 197 Pa. 413.

The first question to be looked into at a meeting of stockholders is whether or not a *quorum* is present. The charter or by-laws of the corporation may determine what shall constitute a quorum, and if they are silent on the subject, a majority in interest of the stockholders must be present in person or by proxy. No rigid formality is required at corporate meetings in order to make them legal, but it is desirable to have everything conducted in an orderly way. The president of the concern may act as chairman, but frequently some one is chosen for this purpose from the ranks of the ordinary stockholders. Some one should also be appointed to take minutes of the meeting. Where an election is to be held it is preferable to have all the proceedings conducted by disinterested members. The mere fact, however, that some of the candidates take charge of the election does not make it illegal.

Most corporate meetings are called for the purpose of conducting an election. The act of April 29, 1874, provides that no person acting as judge or officer holding an election for corporations chartered under it shall enter on his duties until he takes and subscribes an oath or affirmation. This must be made before a judge, alderman, justice of the peace, notary or other person qualified by law to administer oaths. The oath or affirmation is to the effect that the person taking it will discharge the duties of his office or appointment with fidelity and will not receive any vote but such as he believes to be legal. If any such judge or officer wilfully violates his oath or affirmation, he is subject to the penalties imposed by law upon the officers of the public state elections for violating their duty. If an election is held in violation of the act of 1874, or is invalid for any other reason, it may be set aside, and a new election ordered by the Court of Common Pleas of the proper county, upon the petition of no less than five stockholders supported by proof satisfactory to the court. Every stockholder has a right to object to an attempt at casting a vote by a person who is not fully entitled to do so. In order to prepare himself for challenging improper votes, a member has the right to copy the membership list in advance of the election. This was decided in the cases of *McClintock v.*

Young Republicans (1904), 210 Pa. 115, and *Oil Exchange v. Witherop* (1896), 2 Super. 508.

(C) *The business transacted at meetings of corporate members.*

The act of May 14, 1891, provides that the business of every corporation created under the act of 1874, or accepting its provisions, shall be managed and conducted by a president, a board of directors or trustees, a secretary or clerk, a treasurer, and such other officers, agents and factors as the corporation authorizes for the purpose. Officers in most corporations may also be directors, and receive any compensation for their services as officers that they may in their capacity of directors agree to give. If they grossly abuse their powers, and pay themselves amounts which are vastly disproportionate to their services, the injured members may invoke legal proceedings against them. The act of March 31, 1860, however, makes it unlawful for any councilman, burgess, trustee, manager, or director of any public corporation, such as a university, or any municipal corporation, such as the City of Altoona, or of any other public institution, to be at the same time a treasurer, secretary or other officer, subordinate to the president and directors, who shall receive a salary therefrom, or to be the surety of such officer. In the case of small corporations for profit organized by only three persons, it becomes necessary to have all the members on the board of directors, and usually each member has an official position besides. Sometimes, only two officers are appointed, first, a president, and, second, a secretary and treasurer. The act of 1874 requires the president to be chosen from among the directors, but no other officer, except perhaps the vice-president, need be a director. The charter may provide for any number of directors, not less than three.

The act of May 14, 1891, directs that the directors or trustees shall be chosen annually by the stockholders or members at the time fixed by the by-laws, and shall hold their office until others are chosen and qualified in their stead. The manner of such choice, and of the choice and appointment of all other agents and officers of the company shall be prescribed

by the by-laws. It is not necessary to have the entire board of directors elected afresh each year. We have seen that a member has the right to accumulate his votes for any favorite candidate, and in order to prevent a small minority interest from making trouble in corporate affairs, some companies take advantage of the act of May 23, 1887. This statute directs that a provision may be inserted in any charter or amendment of a charter for a corporation of the first class that the directors, managers, trustees, vestrymen or other governing body may be elected in detachments. A half, a third, or a fourth of the whole number may be elected each year, the distribution to be made in accordance with the charter. The act of June 17, 1887, makes a similar provision for corporations of the second class, and all other corporations which have stockholders. The stockholders, at a meeting called for the purpose, may decide whether or not to classify the directors, and elect them in detachments.

A *woman*, single or married, may be elected as a director or officer of a corporation, just as she may be one of the original organizers of it. The act of 1874 does not require a director to be a stockholder, but the charter or by-laws of a corporation may prescribe that none but stockholders shall be eligible to the board of directors.

The time and place of holding the annual election for directors is usually prescribed by the by-laws. The act of May 31, 1887, allows any Pennsylvania corporation to determine by the vote of a majority in interest of its stockholders, at a meeting called for the purpose, the time of holding the annual meeting to elect officers. This does not, however, apply to certain old corporations chartered before the year 1874.

In addition to the election of corporate directors or managers at the annual meeting of stockholders or other members, the latter must be called on to vote on certain extraordinary occasions. Thus when the capital stock of the company is to be increased beyond the existing charter limit, the consent of its members must be obtained, at a meeting called for the purpose. Likewise, when the capital is to be reduced. On this topic,

see the act of April 22, 1905. Likewise, when the corporation is to be merged and amalgamated with another corporation. Likewise, when it is to cease active operations, and to turn over its property and franchises to another concern under a lease or similar arrangement. Likewise, when it is to be dissolved by voluntary abandonment of its charter.

Any proposed amendment to the charter should be submitted to a vote of the members, for the charter constitutes the fundamental contract among the incorporators. Usually a majority vote of the members at a meeting called for the purpose is sufficient to authorize the amendment. Since the charter is granted by the state, something of the same formality as was gone through when the charter was originally obtained must be re-enacted in order to alter it. The amendment does not take effect until the approval of the public authorities is secured.

The act of February 9, 1901, as amended on April 22, 1905, provides that the *capital stock or indebtedness, or both*, of any corporation created by general or special law, may, with the consent of the majority in interest of its stockholders, be *increased* to such an amount in the aggregate of each, without regard to the amount of the other, and *regardless of limitation* upon the amount of either, prescribed in any general or special law regulating any such corporation, as it shall deem necessary to accomplish, carry on and enlarge the business and purposes of such corporation. Such increase may be made at once or from time to time, as the majority in interest of the stockholders shall determine. Upon the authorizing of any such increase of indebtedness by the stockholders of such corporation, it shall be lawful for the corporation to secure payment of the principal or interest, or both, of all or part of such indebtedness, by mortgage, deed of trust, or other pledge or conveyance, by way of security, of all or any part of its real or personal property, rights, privileges and franchises, and in such manner, and upon such terms, as its board of directors may determine. The act goes on to provide two methods for obtaining the consent of the stockholders. It should be borne in mind that whenever the consent of stock-

holders is required to make certain corporate action valid, their consent must be obtained in a regular way. The statute, for instance, which permits one corporation to merge with another, prescribes a method for obtaining the consent of stockholders of each company to the merger. If there were talk of increasing the capital of a company, and a majority of the stockholders, when approached privately by the directors, expressed themselves in favor of the increase, this would not justify the directors in going ahead with it. There must be a corporate meeting, duly called. At such a meeting the stockholders or other members act in their corporate, or collective, capacity, and not as mere individuals. The act of March 24, 1903, provides certain regulations for the holding of these corporate meetings. See the act of May 21, 1889, as to mortgages which may be made by certain corporations.

The act of February 9, 1901, so far as it relates to increasing a company's indebtedness, repeals a provision of the act of 1874. This provision forbids a corporation to increase its indebtedness beyond the amount of its capital stock, until the amount of its capital stock subscribed shall be fully paid in. The act of 1901 does not require stockholders to be consulted in the case of indebtedness contracted in the usual course of corporation business. In *Hardware Co. v. Phalen* (1889), 128 Pa. 110, it was held that the directors of a manufacturing company may mortgage corporate real estate to secure a debt incurred in the course of its usual business in improving the company's property without calling a stockholders' meeting. See also *Hardware Co. v. Roland* (1889), 128 Pa. 119.

Even a majority of the members, assembled at a corporate meeting, have no power to trample on the rights of a small minority. In the case of business companies the object is to make money, and a wide latitude is allowed to a majority interest, if they decide to turn the corporate enterprise into new avenues of profit. If they act in good faith, according to prescribed procedure, they may overrule the wishes of a dissenting minority. In the case of corporations which are not for profit, it may violate the basic principles on which a concern is established to permit a majority to switch the others off in

a new direction. In the case of *Sutter v. Reformed Dutch Church* (1862), 42 Pa. 503, the court refused to let a majority of the members of a church corporation withdraw the corporation from its connection with the Reformed Dutch Church of North America. The majority must direct and control consistently with the general and special laws of the organism or association, of which they are component parts. Perhaps nothing less than a unanimous vote can justify a complete departure from the original purpose of such a corporation.

(D) *The right of a member to inspect corporate books.*

Although an ordinary member of a corporation has little voice in the active management of its affairs, he usually has a right to know what his representatives are doing. The original incorporators may provide that members shall not enjoy this right, but unless it has been expressly waived, you may take its existence for granted. In the case of *Phoenix Iron Co. v. Commonwealth* (1886), 113 Pa. 563, George H. Sellers, a shareholder of the iron company, applied to the court to compel the company to produce its books and papers for inspection. No dividends had been declared for nine years, although the company enjoyed a large business. Sellers charged the people in control with abusing their position to advance their personal interests, by voting themselves large salaries, and in other ways. He wanted to see the books, in order to prepare for hostile legal proceedings. Sellers had applied first to the directors and to the president for permission to inspect the corporate records, but was refused. The court upheld him, and stated that, unless the charter provides otherwise, a shareholder has the right to inspect corporate books and papers, and to take minutes from them for a definite and proper purpose, and at reasonable times. Such a right is, of course, not to be used to gratify curiosity, or for speculative purposes. It must be exercised in good faith and for a specific, honest purpose, and where there is a particular matter in dispute seriously affecting the welfare of the stockholder who asserts it. In the case of *Commonwealth v. Phila. & Reading R. R. Co.* (1893), 3 D. R. 115, it was held that for a proper purpose every stockholder

has the right to inspect and take a copy of the list of stockholders. This list may be obtained with the object of getting proxies from the stockholders for use at corporate elections. See also the following cases: *Commonwealth v. Pa. R. R. Co.* (1897), 6 D. R. 266; *Neubert v. Water Co.* (1905), 211 Pa. 582; *Investment Co. v. Eldridge* (1893), 2 D. R. 394. Every railroad and canal corporation is obliged by the Pennsylvania Constitution to keep a list of its stockholders in its office, open to the inspection of stockholders and creditors.

CHAPTER XXX.

THE LIABILITIES OF STOCKHOLDERS AND OTHER MEMBERS OF CORPORATIONS.

One of the main objects in forming a corporation is often to limit the personal liability of the members. As a rule, membership in a corporation does not entail any responsibility except what the member plainly agrees to assume. A reasonable man who becomes a member of a corporation understands that he thereby subjects himself to its constitution and such regulations as may be required to govern the concern. Many corporations of the first class under the act of 1874 wisely compel every member to sign an agreement at the time of his admission, promising to obey the constitution and by-laws. This practice would be inconvenient in the case of many companies organized for profit, so it is very rarely adopted by corporations of the second class. Whether or not it is adopted, the result is generally the same, for the constitution and by-laws are considered by the courts to embody the terms of agreement among the corporate members. It goes without saying that any other contract by which a corporate member assumes additional liability is binding upon him. For instance, sometimes a number of members of a corporation agree together to raise a fund for it, or to guarantee it against loss in a certain venture. The general rule is that unless an obligation is imposed upon a member by the constitution and by-

laws, he is subject to no liability beyond what he clearly and specifically promises to assume. This rule should be read in the light of what is stated below.

(A) *Liability on stock subscriptions.*

In the third chapter, under rule 6, something was said about the liability of subscribers to stock. This is the most serious obligation incident to membership in a corporation. Most corporations of the first class do not issue stock, and the pecuniary obligations assumed by members are generally confined to the payment of dues. In the case of stock companies, a member's liability varies widely in accordance with the particular amount of stock subscribed for or held by him. In the next sub-division of this chapter we shall consider the liability of a stockholder who was not the original subscriber to the stock standing in his name. At present, we shall treat of the obligation assumed by one who agrees to take stock from the corporation itself. In the third chapter, under Rule 6, it was mentioned that an agreement to take stock in a proposed corporation must be in writing, and may be revoked by a subscriber before the corporation is actually formed. The courts are unwilling to hold a subscriber liable without clear proof of his consent. This rule was applied in the case of *Fair Association v. Greer* (1899), 11 Super. 103. Greer signed the following promise, along with twenty-six others: "We, the undersigned, do hereby subscribe to the capital stock of the Southwest Pennsylvania Fair, the number of shares of the par value of \$25 set opposite our several names, and we do hereby promise and agree to pay for the same as follows—the sum of \$5 per share on the signing of this agreement, and \$5 per share on the first of each and every month thereafter until the same is fully paid. It is understood that no one person shall be allowed to subscribe for or hold more than four shares of said stock." Later the fair company was chartered. Fairs were held, and annual passes were furnished to Greer and the other stockholders. Greer was appointed one of the auditors of the company. When he was sued on his subscription, he

swore that he had no recollection of ever having used the annual passes or acted as auditor. It did not appear that he had returned the passes or declined the appointment as auditor. The court refused to hold Greer liable, partly because the paper which he signed failed to express a purpose on the part of the subscribers to proceed to form a corporation. The mere use of the words "capital stock" in such a document is not conclusive, for these words may also be employed to describe the interest held by a member of an unincorporated association, or even of a partnership. Again, the purpose of the enterprise to be entered upon was not expressed in the paper, save in the statement of the name, "The Southwest Pennsylvania Fair." The carrying forward of such a project does not necessarily involve the creation of a corporation. It was decided that there was no sufficiently clear proof of Greer's intention to subscribe to corporate stock.

On the other hand, in the case of *Jeannette Bottle Works v. Schall* (1900), 13 Super. 96, the following subscription was held to be enforceable: "Whereas, The citizens of Jeannette are forming an association to be chartered under the laws of Pennsylvania as the Jeannette Bottle Works, the capital stock of said company to be \$25,000, consisting of 1,250 shares of \$20 each—in pursuance of the above, we, the undersigned citizens of Jeannette borough and vicinity, agree to subscribe for the number of shares (at the amount of \$20 per share) set opposite our respective names. We further agree to pay for the shares so subscribed by us in the following manner, to wit, one-fifth of the amount so subscribed to be paid when the charter for said company is obtained, one-fifth in 30 days from date of charter, one-fifth in 90 days from date of charter, one-fifth in 5 months from date of charter, one-fifth in 7 months from date of charter." About one hundred persons signed this paper, among them Schall, who was held liable on his subscription. Schall contended that a corporation cannot, after its organization, maintain a suit to enforce subscriptions to its capital stock made before the incorporation. He argued that the corporation was not a party to the contract. The court answered that when the company contemplated by the

subscription paper has been duly organized, it becomes the legal representative of all the subscribers, and is vested with the power to enforce the contract. The organization of the corporation becomes complete when it is ready to file a proper application for a charter in the office of the Secretary of the Commonwealth. Upon the filing of this document, the subscriber's obligation becomes final, and he cannot afterwards withdraw. Schall wanted to prove that he was induced to sign the contract upon certain conditions. The court decided that even if the promoter who obtained his subscription had agreed to the conditions for which Schall stipulated, Schall would not be allowed to rely upon them, unless they were expressed in writing in the subscription agreement. A subscription is not only an undertaking for the use of the proposed corporation. Each individual subscriber is interested in the subscriptions made by others, and has the right to demand that all subscription contracts shall be enforced according to their expressed provisions. When a party has signed an unconditional subscription agreement, in which many other persons join, he cannot escape liability to the corporation by showing that his subscription was subject to a verbal condition, unless he shows also that every other subscriber assented to his making the subscription a conditional one, or that all the subscriptions were made subject to the same verbal condition. See also *R. R. Co. v. Conway* (1896), 177 Pa. 364.

This rule simply means that a written contract cannot usually be contradicted by proof of an inconsistent verbal agreement. It does not mean that stock subscriptions may not be made subject to a condition, if the condition is properly expressed. The written agreement among the subscribers to stock of a corporation proposed to be formed under the act of 1874 is the creation of the associates. It may embrace any condition which does not involve a violation of law or of the rights of future creditors. It would be illegal for the subscribers to agree that if the company should fail no subscriptions should thereafter be binding. This would work injustice to creditors. The case of *Hamilton v. Railroad Co.* (1891),

144 Pa. 34, decides that a condition that a certain subscription should not be binding unless all the capital stock should be subscribed for, would not hold good as against creditors of the corporation. It would be good as against the corporation itself, provided it were properly inserted in the subscription agreement, or assented to by all the other subscribers.

A verbal subscription to stock may be upheld where the subscriber's conduct estops him from objecting that it was not written. In the case of *Brick Co. v. Dyer* (1898), 187 Pa. 470, Dyer was sued on a verbal subscription for \$5,000 of the company's capital stock. Twenty thousand dollars worth of stock was to be issued, and Dyer knew that the money to be raised in this way was needed for improvements. On the faith of his and of the other subscriptions, the company made contracts, and put up machinery. Dyer urged the selection of particular machinery, and knew all the facts just stated. When payment for the stock he had agreed to take was demanded, he promised to pay later, and never repudiated the contract until suit was brought against him. The court decided that he could not question the validity of his verbal contract, since he had knowingly permitted the company to incur expense on the faith of it.

It appeared also that when Dyer originally agreed to subscribe, he told the secretary of the company to put him down for \$5,000. A few minutes thereafter the secretary entered the subscription in the minute book. The Supreme Court stated that the secretary's act in noting the subscription was virtually the act of Dyer himself, because it was done pursuant to his expressed direction. The court declined, however, to decide whether or not such a subscription would have bound Dyer. The decision against him was rested on the doctrine of estoppel. See also the case of *R. R. Co. v. Cowell* (1857), 28 Pa. 329, and that of *Shellenberger v. Patterson* (1895), 168 Pa. 30.

If a corporation issues its shares to subscribers for less money than their par value, the subscribers are liable to make up the difference between what they have paid and par. This liability cannot be escaped by an agreement that the shares

shall be considered as paid in full. Such an agreement savors of fraud. Creditors of the corporation would have reason to complain, if the organizers of a concern with \$20,000 capital could pay only \$10,000 into the corporate treasury, and legally issue the entire capital stock to themselves as "full paid." A corporation may, however, issue full paid shares in exchange for patents, lands, merchandise and other kinds of property. Sometimes a large number of full paid shares are issued to one of the organizers in return for a patent or some other consideration, and he then "gives" some of his stock to the other organizers. Where the patent or other property is overvalued, the stock of the company is "watered," but the transaction cannot usually be set aside without proof of a fraudulent conspiracy to overvalue the property. See *Rehfuss v. Moore* (1890), 134 Pa. 462.

(B) Release of a stockholder's liability by subsequent agreement with the corporation.

After the corporation has been organized, *it cannot release a subscriber from liability without a sufficient consideration.* The rights of other subscribers and of stockholders to have every subscription enforced must be respected. In the case of *Railroad Co. v. Bily* (1899), 11 Super. 144, Bily was sued on his subscription to twenty shares of the company's stock, of the par value of \$50 each. Bily had paid an assessment of \$5 per share at the time he subscribed, and was sued for a second assessment of the same amount. He had received from the company a certificate for two shares, and contended that his original payment of \$100 had been applied to a settlement for these two shares in full, and that he had been released from his obligation to pay the balance of his subscription, \$900. There were more than twenty other stockholders, and the company had a funded indebtedness of \$41,000. Under such circumstances, the court held that it was not within the power of the president and secretary or even of the board of directors to release Bily without a sufficient consideration. The assets of the company cannot be given away even by the direc-

tors. See also the case of *R. R. Co. v. Stewart* (1861), 41 Pa. 54.

(C) *Liability of original subscribers and other stockholders to pay assessments.*

When the subscription to stock is not payable either at once or at some definite time in the future, the directors should make a formal assessment before taking any legal measures to enforce payment. This is termed "making a call," and it is good practice for the board to give the stockholders, if possible, at least one month's notice before the time for paying the assessment.

The act of May 9, 1889, provides that all subscriptions to the capital stock shall be paid in such instalments and at such times as the directors may require, and if default is made in any payment the person or persons in default shall be liable to pay, in addition to the amount so called for and unpaid, interest at the rate of one-half of one per cent per month for the delay of such payment. The directors *may cause suit to be brought for the recovery of the amount due, with interest as aforesaid, or may cause the stock to be sold.* The act of 1874 provides that if any shareholder neglects to pay a sum duly assessed thereon, for thirty days after the time appointed for payment, the treasurer of the company may sell by public auction a sufficient number of the shares to pay all assessments then due, with necessary and incidental charges thereon. The treasurer shall give notice of the time and place appointed for such sale, and of the sum due on each share, by advertising the same three weeks successively before the sale in some newspaper published in the county. See the case of *R. R. Co. v. Fittler* (1869), 60 Pa. 124, in which it was held that where a stockholder has agreed to pay instalments at a certain future time, his stock may be sold if he fails to pay on time without notice to him. See also the case of *Association v. Kountz* (1905), 29 Super. 110.

The remedy to enforce payment of a stock subscription which is adopted when it would not pay to sell the subscriber's shares in the open market is to sue the subscriber. A ques-

tion sometimes arises as to *the length of time within which suit must be brought*. In the case of *Cook v. Carpenter* (1905), 212 Pa. 165, it was decided that the period of six years, which outlaws an ordinary claim, does not begin to run from the date of the original subscription, where it is not immediately payable. Cook was one of the assignees for the benefit of creditors of the Chestnut Street Trust and Saving Fund Company. In 1899 the assignees sued a number of stockholders for an unpaid balance due on their subscriptions, which had been made in 1888. All the calls made in 1888 had been paid, and no further call for the unpaid portion of the stock had ever been made by the directors. The court stated two rules governing the outlawry of claims. First, *where an obligation calls for the payment of money on demand the statute of limitations begins to run at once*. The bringing of suit is a sufficient demand, and suit must be begun within six years. Second, *where the contract is to pay on the future performance of a condition, or the happening of an event, or at a certain time after demand, there a demand is necessary to give a right of action*. The statute does not begin to run until demand is made. Where a stock subscription is not presently payable in full, but by its terms is to be payable from time to time as called for by the company, the period of six years does not commence until the directors, or (as in the case of *Cook v. Carpenter*) the assignees levy an assessment. Until such call, there is no obligation on the stockholder to pay. If the enterprise is successful, and the original provision for capital is sufficient to meet all needs, the call may never be made. Apparently, however, if a corporation should fail, the assignees must make an assessment within six years from the time when the company ceases to do business.

In another case with the same title, *Cook v. Carpenter* (1905), 212 Pa. 177, James S. McCord, a stockholder of record on an insolvent company's books, tried to escape liability by showing that he had transferred the stock. He sold fifty shares at public auction, and Richard L. Carpenter bought and paid for them. Under the corporate rules no transfer

on the company's books could be made at once, because the transfer books were closed after the declaration of a dividend, and pending the payment of it. Meanwhile the company failed, and the transfer, therefore, was never actually made. After Carpenter had paid the auctioneers, the latter sent McCord's certificate, with a blank power of attorney, to the company's office, where a clerk made the entry on the books as follows: "Transferred by James S. McCord to Richard L. Carpenter 50 shares of stock." Later, however, the auctioneers were informed that the books were closed, and the transfer was not further recognized. No certificate was issued to Carpenter.

The act of 1874, under which the company was chartered, provides that shares shall be transferable on the books of the company, "subject to such regulations as the by-laws may prescribe," and the by-laws of this insolvent company prescribed that no transfer should be made while the books were closed. While the ownership of the certificate may have been transferred from McCord to Carpenter, as between those two parties, the situation was different so far as corporate creditors were concerned. The company's insolvency fixed these creditors' rights, and the corporate books are recognized as the best evidence of the responsible ownership of the stock. The tendency is to treat them as conclusive on that point. If the sale to Carpenter and the order to the company to make the transfer had been made while the books were open, the mere neglect or even the refusal of the company to make the proper entries would not, perhaps, have been sufficient to prevent McCord from being released. In this case, however, the refusal of the company was based upon a by-law, and the court decided that the transfer must be complete and in accord with the by-laws before the liability of McCord, the transferor, could give place to that of Carpenter, the transferee.

If McCord had been one of the original subscribers, he would always have remained liable on his subscription, although in case the transfer of his 50 shares had been legally completed he would have had a right of recourse against Carpenter.

He would have had a right of action against Carpenter to reimburse himself, because the assignment of stock involves an implied undertaking on the part of the purchaser to relieve the seller from future liability thereon. *Lichten v. Verner* (1899), 8 D. R. 218.

The foregoing paragraph is based upon the supposition that McCord was one of the original subscribers and that the transfer to Carpenter had been completed according to the corporate by-laws. Now suppose that McCord was not a subscriber, but had bought shares from some other stockholder. His liability would cease upon the proper transfer of the stock to Carpenter on the company's books. *While the original subscriber is liable for all assessments upon his former shares, after they have been transferred out of his name on the corporate books, a subsequent holder is liable only on calls made during the period when the corporate records show him to be the owner.*

(D) *Liability of stockholders for certain corporate debts.*

The act of 1874, as amended by that of April 17, 1876, provides that the stockholders of a corporation organized under it shall be liable in their individual capacity, to the amount of stock held by each of them, for all work or labor done to carry on the operations of the said corporation. No stockholder is personally liable for payment of any such corporate debt, unless suit is brought against him within six months after the debt falls due. In the case of *Bower v. Chemical Co.* (1902), 20 Super. 33, it appeared that Bower had done work for the chemical company in 1896 and 1897. He sued the company and John H. Hayes, one of its stockholders, in 1900. He contended that his right of action against Hayes remained in force until six months from the date when it was finally determined that the chemical company, the primary debtor, was insolvent. The court, however, decided that suit must be brought against a stockholder within six months after the debt originally falls due. The remedy against the stockholders is an extraordinary one, and is to be strictly construed. The liabilities treated in this and in the following paragraph are distinct from the liability of a stock-

holder owning shares whose par value has not been fully paid into the corporate treasury.

The act of 1874 also directs that if any part of the capital stock of a manufacturing company, (or of certain other companies therein mentioned), is withdrawn and refunded to the stockholders, before the payment of all the debts of the company contracted previously to the recording of a copy of the vote to withdraw part of the capital in the office of the Recorder of Deeds, all the stockholders of the company shall be jointly and severally liable for the payment of such previous debts. The stockholders of manufacturing and certain other corporations under this act are personally liable for all sums of money due the laborers, clerks and operatives, for services rendered within six months before demand is made upon the corporation, and its neglect or refusal to pay for same. The act provides also that manufacturing and some other companies may issue quotations of certain "special" stock. Until the special stock is fully redeemed, the general stockholders are personally liable for all corporate debts and contracts. The provisions mentioned in this paragraph apply to most corporations of the second class.

CHAPTER XXXI.

THE RIGHTS AND OBLIGATIONS OF CORPORATE DIRECTORS.

In the twenty-ninth chapter considerable was said about the election of directors and the qualifications necessary to fit one for such positions. See also *Commonwealth v. Detwiller*, set forth in Chapter XXVII. Sometimes these functionaries are called trustees or managers, and in almost every corporation there is a board of such persons who are the direct representatives of the stockholders. The directors usually appoint the president and other principal executive officers, who in turn usually appoint their own subordinates.

(A) The rights and powers of directors.

The directors are the general agents of the corporation. Their authority is usually defined in the charter or by-laws. In

the case of a business corporation, the board is usually considered to have, in the absence of a provision to the contrary, the following powers: to issue the corporate stock and make contracts concerning it; to make assessments upon stock which is not fully paid up; to declare dividends; to start actions at law on behalf of the company, and to compromise or push them to a conclusion; to make contracts concerning the corporate business, and, in a word, to *direct* its affairs. Something is said upon this topic in Chapter XXIX.

A director of a corporation, like a partner, cannot receive pay for his services, without either an express contract or a regulation in the charter or by-laws to that effect. This was decided in the case of *Grafner v. Railway Co.* (1903), 207 Pa. 217. Certain directors had issued stock to themselves in return for services rendered to the corporation. The stock came into Grafner's possession, and he sued to compel the corporation to transfer it to his name. The court upheld the defense of the corporation that the stock had originally been issued without consideration, even against Grafner, for it appeared that he knew the facts of the case when he took the stock. He was not, therefore, an innocent holder. In the case of *Loan Association v. Stonemetz* (1858), 29 Pa. 534, Stonemetz was refused compensation for services, although a resolution had been *subsequently* passed by the association to pay him for them. He had been elected chairman of a certain committee of directors, and had done a great deal of work in that capacity for two years. The court held that he could not base his action against the association upon its subsequent resolution, since no consideration had been given by him in exchange for the passage of the resolution. Directors are frequently allowed \$5 or \$10 for attendance at each board or committee meeting. It is wise to have this allowance authorized in the by-laws.

In the case of *Bergdoll v. Brewing Co.* (1901), 10 D. R. 173, the following by-laws of the brewing company came before the court: "No director, as such, shall receive any salary for his services, but this is not to be construed to preclude any director from holding any other office in the

company and receiving compensation therefor, or for performing any special services for which compensation may be allowed, provided that no director shall be chosen to any office, for which compensation is allowed or such compensation fixed, except by a majority of the whole number of directors." It was held that in the absence of authority conferred by the charter or by-laws, or by a statute, a majority of the board could not create salaried offices other than those existing under the charter and by-laws, and elect themselves to such offices. Furthermore, the court suggested that when a vote of the board is taken upon the question of putting one of the directors into a salaried office, the ballot of that particular director shall not be counted.

The act of 1874 directs that in case of the death, removal or resignation of the president or any of the directors, treasurer or other officer, the remaining directors may supply the vacancy thus created until the next election. It is not absolutely necessary to fill vacancies at once. In the case of *Wright v. Commonwealth* (1885), 109 Pa. 560, it appeared that the cumulative system of voting had been employed at an election with the result that only five of the candidates were elected. There were seven places on the board, but the election of the five men was valid. These five constituted a quorum, and their power to act was not impaired by the failure to fill up the board.

When the number of directors is reduced below a quorum, their power is suspended. *A quorum consists of a majority of the entire number of directors provided for in the charter.* In the case of *Curry v. Cemetery Association* (1897), 5 Super. 289, the constitution and by-laws of a corporation which permitted less than a majority to constitute a quorum were declared illegal. Six directors were provided for, three of whom were to make a quorum. The act of 1874, as amended by the act of May 14, 1901, provides that a majority of the whole number of directors or trustees shall be necessary for a quorum. Accordingly, the appointment of a superintendent at a meeting where only three directors were present was held not to bind the corporation. Neither would the independent

action of several directors, outside of a board meeting, validate the agreement, unless the board had given them authority. *The directors, like the stockholders, act in their collective capacity.* None of them has any individual authority merely because he has been elected to the board. Directors' meetings should usually be held in Pennsylvania. If a majority of the directors are citizens of any other state, meetings of the board may be held at any place, whether in Pennsylvania or elsewhere, as such majority may from time to time appoint.

The by-laws should allow the directors to depute some of their number, either singly or in *committees*, to manage important matters. A single director may possess a large measure of authority which is thus legally transmitted to him, but he derives it from the action of the board in meeting assembled. In considering what authority is possessed by any director, officer or other corporate agent, we should always be careful to trace it to its source. Many acts on the part of self-styled corporate agents have been held not to bind the corporation, because the agents were not formally authorized to represent it.

Frequently a corporation is chartered with directors who own but a few shares, and who promptly resign in favor of those who are more heavily interested. This is perfectly legal, because it is permissible to change the directors at any time. One who has been elected for a certain term cannot, however, be forced out of office unless he misbehaves himself. Even after the expiration of a director's term, he holds over until his successor is chosen. The courts recognize the necessity of having some responsible governing body.

The board of directors are the general representatives of the members, and vested with the power of conducting all ordinary corporate affairs. Those who are responsible for the success of the corporation should see that the board meetings are regularly held, and that minutes are preserved of each meeting. These minutes should show affirmatively that a quorum was present. They should also state various important details in the conduct of the meeting: whether the meeting was a regular or special one, who acted as chairman, what

resolutions were passed, what reports were received and how they were treated, what committees were appointed. By transacting business with attention to formality, the directors may save themselves from future criticism, and perhaps from serious trouble and pecuniary loss.

(B) *The obligations and liabilities of directors.*

As directors are merely unpaid representatives of the corporate members, a great deal should not be expected of them. Like any other agent, a director is liable for a breach of the confidence reposed in him. It is folly, however, to consider that he must devote a very large portion of his time and energy to work for which he receives no compensation. Neither does he insure the corporation against the consequences of his honest actions. If directors, acting within their authority, take certain measures in the interest of the corporation which turn out disastrously, they cannot be held liable. They are responsible for gross negligence or dishonesty, but not for the mere failure of any corporate undertaking. This was decided in the case of *Commonwealth v. Anchor Building and Loan Association of York* (1902), 20 Super. 101. The association failed, and the president and other directors presented claims against it before the auditor appointed to distribute its assets. Other creditors objected, accusing the directors of negligence in managing the corporate business. The claims of these directors arose upon judgments obtained against them as indorsers of notes on which the association borrowed money. The amount thus borrowed by the association exceeded its lawful limits, but this did not exclude the directors from sharing in the funds of the insolvent concern. The borrowed money had not been turned to improper uses, and presumably it formed part of the assets distributed by the auditor.

Another objection against the allowance of the directors' claims was that they had made loose and ill secured loans. This objection was also dismissed. The by-laws authorized the employment of counsel, whose duty it was to search titles and see that all the legal papers were in good shape. The value of the security offered by borrowers was required by the

by-laws to be submitted to a committee. *The board had followed these by-laws.* Members of a governing body have a right to rely upon a report made by a committee upon such matters, and are protected when the committee fails to exercise sound judgment. Of course, if the members of the committee made their report without examining the security, they would be personally liable for their own negligence. Not so the other members of the board, unless they had reason to suspect that the committee was disregarding its duty. Furthermore, if the attorney employed to examine titles and prepare documents, proves negligent or dishonest, the board will be protected, if they have chosen him with proper caution.

The directors were also charged with having paid off an old series of building association stock before the earnings really warranted them in declaring it matured. This mistake, perhaps, caused the corporation's failure, but it was decided that the directors had exercised proper care in the matter. They were bound to a diligent observance of duty, and to show a reasonably intelligent skill in managing corporate affairs. *They were, however, neither insurers against insolvency nor expert accountants.* They were not obliged to give the same time and attention to business as a person bestows upon his own affairs. They examined the statements placed before them by the secretary and counsel, who were familiar with building association matters. These statements apparently disclosed a sufficient accumulation of funds to warrant paying off the old series of stock. Their action could not be regarded as fraudulent or grossly negligent, and the directors were not liable for the unfortunate results of their management. They were given small sums for attendance at board meetings, but this did not put them on the plane of salaried employees. In a great many corporations the sum of \$5 or \$10 is given to each director for attendance at meetings. Such insignificant payments cannot impose an obligation on them to put aside their private business and devote a great part of their time to corporate affairs.

Upon the insolvency of a partnership, the members are not allowed to participate in the distribution of firm assets,

until all outside creditors have been satisfied. A partner is regarded as being one of the debtors behind all firm obligations, so he should not be allowed to compete with other creditors for a claim of his own against the firm, and get a proportionate dividend. When a corporation fails, the association, as a collective body, is regarded as being the debtor, and the case mentioned above shows that its members and even its president and directors may receive a dividend upon claims against it, along with outside creditors. See also the case of *Mercantile Co. v. Mining Co.* (1899), 193 Pa. 28.

The act of March 31, 1860, provides that no member of any corporation or public institution, or any officer or agent thereof shall be in any wise interested in any contract for the sale or furnishing of any supplies or materials to or for the use of any corporation, municipality or public institution of which he shall be a member or officer, or for which he shall be an agent, nor directly or indirectly interested therein, nor receive any reward or gratuity from any person interested in such contract or sale. Any person violating the act of 1860 is threatened with forfeiture of his membership in such corporation, municipality or institution, and his office or appointment thereunder, and on conviction thereof shall be fined not exceeding \$500. See Banking Act of May 13, 1876, sec. 21.

There are, however, many contracts which may be made between those interested in the corporation and the corporation itself. In the case of *Warren-Ehret Co. v. Manufacturing Co.* (1901), 198 Pa. 412, an attempt was made to set aside a sale of land to a corporation by one of its promoters. Under the agreement of sale this man and two of the other promoters, who had done work upon the land, were to receive a portion of the purchase money in cash and the remainder in the capital stock of the company. By an agreement of the three promoters among themselves, a portion of the cash was to go to the man who had owned the land, while the remainder of the cash and the stock were to be received by the other two promoters. The auditor before whom these facts were proved thought that they showed overvaluation of the land and fraud, especially as one of the promoters was the president of the

corporation and a director. The court, however, upheld the sale on the ground that no bad faith had been proved.

A corporate officer should not attempt to make a contract between himself and the corporation, without consulting the other officers. Such an attempt is invalid, unless properly ratified afterwards by the corporate authorities. This is like the case of a partner making an agreement between himself and the firm, without consulting his co-partners. A corporate agent should be careful not to confuse his personal affairs with those of the concern which he represents. In the case of *Dent v. Huntley* (1897), 182 Pa. 607, a director, who had been authorized to purchase logs for his company, and who had made a written contract of purchase, attempted to set this aside, in order to sustain a sale of the logs to himself. He wanted to resell them to the corporation at a profit, and the court held that he was bound to show clearly that he acted in good faith. As he failed to show this, he lost his suit. See also the following cases: *Huntley v. Goodyear* (1897), 182 Pa. 613; *Coal & Iron Co. v. Humes* (1893), 157 Pa. 278; *Swentzel v. Bank* (1892), 147 Pa. 140; *Granger v. Pigott* (1901), 10 D. R. 327; *Hill v. Frazier* (1853), 22 Pa. 320; *Kauffman v. Keifer* (1896), 5 D. R. 620. If a corporation is insolvent the directors who hold claims against it must not use their power to obtain preferences at the expense of the other creditors. *Hill v. Mfg. Co.* (1901), 198 Pa. 446.

Just as the same man may be a member of two different firms, so he may be a member, director or officer of two different corporations. If he deals with one concern on behalf of the other, he should be careful to be thoroughly fair to both parties, and to let each party understand that he is interested in the other. Many companies which do business outside the state from which they have obtained their charter organize a subsidiary company to hold real estate and take charge of other matters in the foreign state where they do business. Sometimes the boards of directors of both companies are composed of the same members, but this does not make the companies identical, or prevent them from dealing with one another, provided their transactions are honest and undertaken in good faith.

Ordinarily, no special liability for corporate debts or for the failure of any corporate enterprise falls on the directors, unless they have acted fraudulently or negligently. See the case of *Lincoln Market Co.* (1899), 190 Pa. 124. The act of 1874 provides that if the directors of any company declare any dividend when the company is insolvent, or the payment of which would render it insolvent, they shall be jointly and severally liable for all the corporate debts then existing, and for all thereafter contracted so long as they respectively continue in office. The amount for which they are liable does not exceed the amount of such dividend. If any of the directors are absent at the time of making the dividend, or object thereto at said time, and file their objections in writing with the clerk of the company, they are exempt from such liability. In discussing the powers of corporate members, we saw that under the act of April 22, 1905, amending that of February 9, 1901, the members must approve of certain increases of indebtedness. The act of 1874 apparently makes directors specially liable for such increases in case the stockholders have not given their approbation. See the case of *Magarge & Green Co. v. Ziegler* (1899), 9 Super. 438. The act of July 18, 1863, (reported in Appendix of Pamphlet Laws for 1864, page 1102), provides that before any stockholder or official shall be held liable for corporate debts or other obligations, a judgment must be recovered against the corporation itself, and it must appear that the sheriff has made an unsuccessful effort to satisfy the judgment out of corporate assets. The act of June 12, 1878, provides that if any officer, director, attorney, receiver, broker, member or agent of a public or private corporation shall as such receive or possess himself of any money or other property of the corporation, otherwise than in payment to him of a just claim, and shall, with intent to defraud, omit to make, or cause or direct to be made, a full entry thereof in the corporate books or accounts, he shall be punished by fine and imprisonment. The same act makes it a crime for an officer, director, member, agent or other employee of a corporation, with fraudulent intent, to destroy, alter, mutilate or falsify any of the books, papers, writings or securities belong-

ing to the concern, or to make or concur in the making of any false entry or any material omission in any books of accounts or other documents. The same act makes it a crime for any officer, director, agent or other employee, attorney, broker or member of a corporation to make, circulate or publish, or concur in the making, circulating or publishing, any written or printed statement or account, which he knows to be false in any particular, with intent to deceive any member or creditor of such corporation, or with intent to induce any person to become a shareholder therein, or to advance any money or property thereto, or to enter into any security for the benefit thereof.

CHAPTER XXXII.

THE RIGHTS AND OBLIGATIONS OF THE PRESIDENT AND OTHER CORPORATE OFFICERS.

(A) *The President.*

The chief executive officer of most corporations is called the president. He is usually responsible for seeing that the corporate affairs are kept running, and that the orders of the directors are fulfilled. He is usually the main agent of the corporation in its dealings with outsiders. His powers, like those of any other agent, vary widely in accordance with the nature of his principal's business, and the amount of authority committed to him.

In the case of *Wright's Appeal* (1882), 99 Pa. 425, which was set forth at length in the twenty-seventh chapter, it was held that the president cannot bind the company by a contract to borrow money for it, if it appears that he was never authorized to do so, and that he converted the money to his own use. If he had been authorized to borrow, or if the loan had been subsequently ratified by the directors, the company would have been bound. For a case where a contract made by the president of an incorporated institution was held not binding on the company, see *Workhouse v. Moore* (1880),

95 Pa. 408. It would seem that the president has implied authority to make ordinary contracts for the conduct of the corporate business. Thus, if the company runs a factory, the president, as such, has implied authority to engage hands, to buy materials, and to sell the finished product. Frequently the president's powers are enlarged, either by an express resolution of the board of directors or through the working of the doctrine of estoppel. If he has for a long period acted on behalf of the company without objection from anyone in a way which clearly points to his having very extensive authority, the corporation is afterwards precluded from showing that he exceeded his powers as against an innocent third party.

If the president oversteps the limits of his authority, the corporation should promptly repudiate his action. Even if the action is disaffirmed at once, the corporation cannot retain the benefits received under an unauthorized contract, and also escape the liability imposed by it. The president should protect himself by getting clear instructions from his board as to the line of action which they want him to pursue. He should report what he has done at all board meetings, and secure the approval of the board. In all important matters a formal resolution should be adopted by the directors, and spread on the minutes of the meeting. If he is about to undertake work for which he expects special compensation, he should have this agreed to in advance. See the case of *Bagaley v. Iron Co.* (1892), 146 Pa. 478.

In the twentieth chapter, we saw that an agent who exceeds his authority is personally liable to the third party with whom he deals. A corporation is a complicated organism, with limited powers and with defined methods of procedure. A responsible corporate officer should, therefore, be particularly careful to keep within bounds. A corporate officer, who is faithful to his own duties, cannot be held responsible for the dishonesty or shortcomings of the subordinates whom he appoints in accordance with the authority given him. He must not throw his own work on another's shoulders, however, and expect to shield himself from liability if the work is done improperly.

In the case of most corporations of the second class, the law provides that the president, secretary, treasurer and a majority of the directors shall, after the last instalment of the capital stock is paid, sign and swear to a certificate stating the amount of the capital so paid in. This certificate must be recorded in the office of the Recorder of Deeds of the county where the company's principal office is located.

(B) The Secretary.

The secretary is responsible for the keeping of proper corporate records. If he lets other officers usurp his functions, and does not keep track of affairs, he may subject himself to serious loss. The exact duties of his position may be defined by corporate regulations, and if this is so, he need not concern himself with outside matters. In the absence, however, of such regulations, he should take it upon himself to see that the corporate records are fully and correctly kept. He should also see that the important books of account, and other documents in his charge are preserved in a reasonably safe place.

In the case of most corporations of the second class either the secretary or the treasurer must keep a book at the company's office or principal place of business containing the names, alphabetically arranged, of all persons that are (or have within one year been) stockholders, showing their residences, the number of shares held by each, the date when each acquired his shares, the amount paid on such shares and the total amount of the capital stock paid in. This book must, at the end of the year, be preserved in the company's office for future reference, and must be open, during the usual business hours on each day, to the inspection of all persons desiring to examine it.

(C) The Treasurer.

The treasurer or cashier is the recognized custodian of corporate funds. He should make it his personal business to see that they are properly collected and entered in the corporate books. He should investigate the financial condition of

the bank or other institution where they are deposited. For his own protection, as well as for the interests of his employer, he should keep rigidly enforced some approved system for checking off corporate receipts and expenditures.

Most treasurers find it to their advantage to have it required that corporate checks shall be countersigned. This enables them to divide the responsibility. While he is not usually responsible for a subordinate's negligence, theft or embezzlement, he is liable in cases where the corporation would have been saved from loss if he had not been negligent or corrupt himself. If the treasurer or any other inferior officer learns that the president or directors are embezzling the company's funds, he cannot shield himself from personal liability behind them. He is not a mere automaton, and when he remains silent with knowledge that the company is being wronged, he commits a breach of duty.

A treasurer or other officer who receives no salary is held liable only for gross negligence. *Association v. McGrath* (1893), 154 Pa. 296. All treasurers, as well as other corporate officers who handle much money, should be put under bond, with ample security. Such bonds should be examined at regular intervals, in order to see that they are in good shape. Where a bonded officer is re-elected for another term, his bond usually needs to be renewed.

CHAPTER XXXIII.

THE MERGER AND CONSOLIDATION OF CORPORATIONS.

(A) *Corporations of the first class.*

The act of April 17, 1876, amending the act of 1874, provides that if any two or more corporations of the first class desire to consolidate and merge with each other, or one or more within the other, application shall be made to the Court of Common Pleas of the county where the corporation is situated, into which the other corporation or corporations desire to merge or become consolidated. Suppose, for instance,

that a church corporation established in Delaware County, near the border line of Montgomery County, desires to be merged into a corporation in the latter county. The Montgomery County concern is to swallow up the one organized in Delaware County. The act provides that the Montgomery County court is the one to hear the petition.

The method provided by the act of 1876 for a merger is the same that it provides for an amendment of the corporate charter. The petition which is made to the Court of Common Pleas, should set forth all the facts in the case, and the reasons for making it. It should recite that a meeting of the members was called to consider the question, and that a majority of those in attendance voted in favor of the merger proposed. The corporate seal should be attached, and the petition should be signed by the president and attested by the secretary.

(B) Corporations of the second class.

The act of May 29, 1901, provides fully for the amalgamation of corporations of the second class. This statute as amended on March 31, 1905, reads as follows:

SECTION 1. *Merger and consolidation of certain corporations.*—It shall be lawful for any corporation now or hereafter organized under, or accepting the provisions of, the act, entitled "An act to provide for the incorporation and regulation of certain corporations," approved April twenty-ninth, one thousand eight hundred and seventy-four, or of any of the supplements thereto, or of any other act of Assembly authorizing the formation of corporations, to buy and own the capital stock of, and to merge its corporate rights, powers and privileges with and into those of, any other corporation, so that by virtue of this act such corporations may consolidate, and so that all the property, rights, franchises and privileges then by law vested in either of such corporations, so merged, shall be transferred to and vested in the corporation into which such merger shall be made: Provided, That nothing in this act shall be construed so as to permit railroad, canal, telegraph companies, which own, operate or in any way control parallel or competing roads, canals or lines, to

merge or combine: And provided further, That any corporation formed for the purpose of carrying on any manufacturing business under the seventeenth or eighteenth clause of section two of an act, entitled "An act to provide for the incorporation and regulation of certain corporations," approved April twenty-ninth, one thousand eight hundred and seventy-four, with the powers conferred by section thirty-eight or section thirty-nine of said act, may be merged and consolidated, under the provisions of this act, with any other corporation formed for any purpose provided for in either the seventeenth or eighteenth clause of section two of the act above cited; but nothing in this act contained shall extend or enlarge beyond its former territorial limits the exclusive franchise of any gas or water company.

SECTION 2. *Joint agreement. To be submitted to stockholders.*—Said merger or consolidation shall be made under the conditions, provisions and restrictions, and with the powers herein set forth, to wit:

I. The directors of each corporation may enter into a joint agreement, under the corporate seal of each corporation, for the merger and consolidation of said corporations; prescribing the terms and conditions thereof, the mode of carrying the same into effect, the name of the new corporation, the number and names of the directors and other officers thereof, and who shall be the first directors and officers and their places of residence, the number of shares of the capital stock, the amount or par value of each share, and the manner of converting the capital stock of each of said corporations into the stock of the new corporation, and how and when directors and officers shall be chosen, with such other details as they shall deem necessary to perfect the said consolidation and merger; but said agreement shall not be effective unless the same shall be approved by the stockholders of said corporations, in the manner hereinafter provided.

II. Said agreement shall be submitted to the stockholders of each of said corporations, at separate special meetings, of the time, place and object of which respective meetings due notice shall be given by publication, once a week for

two successive weeks before said respective meetings, in at least one newspaper in the county or each of the counties in which the principal offices of said respective corporations shall be situate; and at said meetings the said agreement of the directors shall be considered, and a vote of the stockholders in person or by proxy shall be taken, by ballot, for the adoption or rejection of the same, each share of stock entitling the holder thereof to one vote; and if a majority in amount of the entire capital stock of each of said corporations shall vote in favor of said agreement, merger and consolidation, then that fact shall be certified by the secretary of each corporation, under the seal thereof, and said certificates, together with the said agreement or a copy thereof, shall be filed in the office of the Secretary of the Commonwealth, whereupon the said agreement shall be deemed and taken to be the act of consolidation of said corporations.

SECTION 3. Upon the filing of said certificates and agreement, or copy of agreement, in the office of the Secretary of the Commonwealth, the said merger shall be deemed to have taken place, and the said corporations to be one corporation under the name adopted in and by said agreement, possessing all the rights, privileges and franchises theretofore vested in each of them, and all the estate and property, real and personal, and rights of action of each of said corporations, shall be deemed and taken to be transferred to and vested in the said new corporation without any further act or deed. Provided, That all rights of creditors and all liens upon the property of each of said corporations shall continue unimpaired, and the respective constituent corporations may be deemed to be in existence to preserve the same; and all debts, duties and liabilities of each of said constituent corporations shall thenceforth attach to the said new corporation, and may be enforced against it to the same extent and by the same process as if said debts, duties and liabilities had been contracted by it. But such merger and consolidation shall not be complete, and no such consolidated corporation shall do any business of any kind, until it shall have first obtained from the Governor of the Commonwealth new letters patent, and shall

have paid to the State Treasurer a bonus of one-third of one per centum upon all its capital stock in excess of the amount of capital stock of the several corporations so consolidating, upon which the bonus required by law had been theretofore paid: And provided further, That new letters patent of such consolidated corporation shall not be issued by the Governor of the Commonwealth until each and every corporation, entering and forming the consolidated corporation, shall have filed with the Secretary of the Commonwealth a certificate from the Auditor General of the Commonwealth, setting forth that all reports required by the Auditor General of the Commonwealth have been duly filed, and that all taxes due the Commonwealth of Pennsylvania have been paid.

SECTION 4. A certified copy of said certificate and agreement, or copy of agreement, so to be filed in the office of the Secretary of the Commonwealth, shall be evidence of the lawful holding and action of such meetings, and of the merger and consolidation of said corporations.

SECTION 5. If any stockholder or stockholders of any corporation which shall become a party to an agreement of merger and consolidation hereunder, shall be dissatisfied with or object to such consolidation, and shall have voted against the same at the stockholders' meeting, it shall and may be lawful for any such stockholder or stockholders, within thirty days after the adoption of said agreement of merger and consolidation by the stockholders as herein provided, and upon reasonable notice to said corporation, to apply by petition to any court of common pleas of the county in which the chief office of such corporation may be situate, or to a judge of said court in vacation, if no such court sits during said period, to appoint three disinterested persons to estimate and appraise the damages, if any, done to such stockholder or stockholders by said consolidation. Upon such petition, it shall be the duty of said court, or judge, to make such appointment; and the award of the persons so appointed, or of a majority of them, when confirmed by the said court, shall be final and conclusive; and the persons so appointed shall also appraise the share or shares of said stockholders in

the said corporation, at the full market value thereof, without regard to any appreciation or depreciation in consequence of the said consolidation, which appraisement, when confirmed by the said court, shall be final and conclusive; and the said corporation may, at its election, either pay to the said stockholder or stockholders the amount of damages so found and awarded, if any, or the value of the stock so ascertained; and upon the payment of the value of the stock as aforesaid, the said stockholder or stockholders shall transfer the stock so held by them to the said corporation, to be disposed of by the directors thereof or to be retained for the benefit of the other stockholders; and in case the value of said stock, as aforesaid, shall not be so paid within thirty days after the said award shall have been confirmed by said court, the damages so found and confirmed shall be a judgment against said corporation, and may be collected as other judgments in said court are by law recoverable.

See also the act of March 24, 1905, which permits a corporation organized under the act of 1874 and its supplements for carrying on any manufacturing business, or for supplying water, or for manufacturing or supplying light, to subscribe for or purchase bonds or stock in any company of the same character, incorporated under the act of 1874 or its supplements, or to guarantee the payment of the said bonds, principal and interest, *or to contract for the use or lease of the property*, real and personal, of such other company. Other Pennsylvania statutes authorize certain other kinds of corporations to lease their property in the manner contemplated by the act of March 24, 1905. The practical effect of many leases made under these acts is to consolidate the company whose property is leased with the leasing company. The latter conducts all the active operations, while the former does little more than maintain its legal existence. The former keeps up its separate corporate organization, and receives for the use of its property a rental which it divides among its stockholders, but it does not usually pursue any active line of business. See the act of April 23, 1903, as to railroad and other transportation companies, and the act of March 19, 1903, as to electrical com-

panies. Where a lease by a corporation involves a transfer of all its property, there should be a meeting of the corporate members to authorize the lease.

CHAPTER XXXIV.

PENNSYLVANIA BONUS AND TAX LAWS; REGULATION OF DOMESTIC AND FOREIGN COMPANIES.

The term "foreign corporations" embraces not only corporations chartered by another nation, but also those chartered by our sister states. National banks and other corporations created under an act of Congress are not considered in the present chapter, because for the most part they are exempt from state interference. The law of Pennsylvania is more favorable in certain respects to corporations created by other states of the Union than to those created beyond our national boundaries. Under the fifth sub-division of the fourth chapter mention is made of a number of acts which permit certain corporations of our sister states to hold title to Pennsylvania realty, subject to certain conditions. No such permission is given to Canadian, Mexican or European corporations. The foreign corporations favored in this matter of holding Pennsylvania real estate include certain manufacturing, quarrying, ice and mineral water companies, also certain navigation, insurance and book publishing concerns. The acts referred to, however, impose limitations upon these foreign companies, which should be respected. Moreover, semi-public corporations, such as railroad and railway companies, chartered elsewhere, cannot enjoy public franchises or exercise the right of eminent domain in Pennsylvania. Any foreign corporation may hold mortgages against Pennsylvania real estate, for mortgages are personal property, and not realty. The act of April 26, 1855, forbids any foreign government or foreign corporation to hold real estate in Pennsylvania unless specially authorized. It is illegal for a foreign corporation to try to evade the law by putting the

title in the name of a trustee. In the case of *Commonwealth v. R. R. Co.* (1891), 139 Pa. 457, it was held that *a foreign corporation may be the owner of the entire capital stock of a Pennsylvania company which holds lands here.* A foreign corporation which lacks the power to hold title to Pennsylvania realty may, nevertheless, *lease land* in this state. *Steam-Boat Co. v. McCutcheon* (1850), 13 Pa. 13.

(A) Bonus and Taxes.

Many companies organized to do business in Pennsylvania obtain a charter from some other state, either to secure more extensive corporate powers than they can get here, or to avoid the heavy Pennsylvania charter fees and taxes. The act of May 3, 1899, requires a bonus of one-third of one per cent on the amount of the capital stock which a Pennsylvania corporation of the second class, except building and loan associations, is authorized to issue, and a like bonus upon any authorized increase of stock. This is the price paid for the charter. The act of May 8, 1901 (P. L. 149), quoted at the end of Chapter XXIV, requires a similar bonus from limited partnership associations organized in Pennsylvania.

The act of May 8, 1901 (P. L. 150), provides that all corporations, limited partnerships or joint-stock associations, except insurance companies, chartered or created by or under the laws of any other state, or of the United States, or any foreign country, whose principal office or chief place of business is located in Pennsylvania, or which have any part of their capital actually employed wholly within this state, shall pay to the State Treasurer, for the use of the Commonwealth, a bonus of one-third of one per cent upon the amount of their capital actually employed or to be employed wholly within Pennsylvania, and a like bonus upon each subsequent increase of capital so employed. The case of *Commonwealth v. Danville Bessemer Co.* (1904), 207 Pa. 302, decides that this act does not apply to capital invested in Pennsylvania before its passage. In the case of *Commonwealth v. Improvement Co.* (1903), 6 Dauphin, 103, it was decided that a foreign corporation is not affected by the statute of 1901 merely because it owns stock in Pennsylvania corporations.

A concern which is to establish plants in a number of states, usually prefers a New Jersey or other foreign charter to one granted in Pennsylvania. The Pennsylvania Legislature is always on the alert to find new ways of taxing corporations. The act of June 8, 1893, imposes a yearly tax of one-half of one per cent upon the actual value of the whole capital stock of every Pennsylvania corporation, joint-stock association, limited partnership or other company, except banks, savings institutions and concerns organized for manufacturing purposes, and certain kinds of insurance companies, for taxing which special provisions have been made. In order that a manufacturing company may avail itself of this exemption, it must be engaged mainly in manufacturing and its charter must clearly show that it was formed with the object of manufacturing. A trading corporation, formed exclusively for commercial purposes, cannot claim the exemption on the ground that part of its capital is invested in manufacturing. Likewise, concerns engaged in brewing or distilling spirits or malt liquors, and such as enjoy and exercise the right of eminent domain are not exempted from the yearly capital tax. Every manufacturing concern is bound to pay the yearly tax of one-half of one per cent on such part of its capital, if any, as may be invested in any property or business not strictly appurtenant to manufacturing. This tax is in addition to the local tax assessed upon its property in the district where the property is located.

The capital stock tax is not imposed upon any part of the capital invested in United States bonds; or in a patent right which is absolutely owned by the corporation; or in tangible property employed in other states. See *Commonwealth v. Railroad Co.* (1891), 145 Pa. 96. The act of June 8, 1893, imposes a similar tax upon such part of the capital stock of foreign corporations and limited partnerships as is employed by them in conducting business in Pennsylvania. The same exemptions that have just been mentioned in connection with domestic concerns are allowed in the case of those organized elsewhere. For instance, a New York manufacturing corporation which runs a mill in Pennsylvania is not liable to the capital stock tax on its

capital employed here in conducting the mill. Throughout this chapter it will be seen that the aim of our legislature is not to discriminate against foreign companies, but rather to subject them to the same taxes and regulations as domestic concerns. See *Commonwealth v. Steamship Co.* (1903), 12 D. R. 363.

Other acts provide for a state tax on the gross receipts of certain semi-public corporations; provision is also made for a tax on the net earnings and income of certain corporations; for a tax on the premiums of insurance companies; for a tax on building and loan associations; and for a tax on banks and bank shares. The state also imposes a tax on certain corporate loans, and requires the corporations in such cases to assess and collect it.

It is usually cheaper to organize a manufacturing corporation under Pennsylvania laws, if nearly all of its capital is to be employed in this state. Likewise, a company which is to exercise public franchises in Pennsylvania or to hold title to Pennsylvania realty should as a rule be chartered here. Some foreign corporations conduct railways in Pennsylvania, and otherwise exercise public franchises here by forming an auxiliary corporation under the laws of this state. The foreign company by controlling the stock of the Pennsylvania concern, may accomplish its object, and, perhaps, save considerable money in charter fees and annual taxes.

(B) *Reports and Registration.*

Yearly report to Auditor General.—The act of May 8, 1901, provides that no corporation, limited partnership or joint-stock association liable to pay bonus under this act shall go into operation or transact any business within this commonwealth without having first made a report under oath to the Auditor General stating specifically:

First. The state or country in which incorporated or created.

Second. The date of incorporation or organization.

Third. The location of its chief office in this state.

Fourth. The name and address of its president and treasurer.

Fifth. The amount of its bonded indebtedness.

Sixth. The amount of its authorized capital stock.

Seventh. The amount of capital paid in.

Eighth. The amount of capital employed wholly in the State of Pennsylvania.

And each of said corporations, limited partnerships or joint-stock associations, shall make a similar report annually thereafter, not later than the thirtieth day of November of each year.

The yearly report to the Auditor General just referred to is for the purpose of enabling him to learn what bonus is payable by foreign companies. The act of June 1, 1889, as amended by that of June 8, 1891, provides for the filing of certain information by domestic and foreign limited partnerships and corporations in the office of the Auditor General. Blanks upon which to furnish the information required by these acts and by the act of May 8, 1901, are supplied by the Auditor General; and the Secretary of the Commonwealth supplies blanks for registry under the act of April 22, 1874, which we shall consider next.

The Pennsylvania Constitution directs that no foreign corporation shall do any business in this state, without having one or more known places of business and an authorized agent or agents in the same, upon whom process may be served. The object of this is to prevent a foreign corporation which does business here from evading taxation and lawsuits in Pennsylvania. The act of April 22, 1874, provides that no foreign corporation shall do any business in Pennsylvania until it shall have filed in the office of the Secretary of the Commonwealth a statement, under the corporate seal, and signed by the president or secretary thereof, showing the title and object of said corporation, the location of its office, and the name or names of its authorized agent or agents therein. The Secretary of the Commonwealth issues a certificate of the filing of this statement, which must be preserved for public inspection by each of said agents, in each of said offices. This statute provides that any person, agent, officer or employee, who shall transact any business in Pennsylvania for

a foreign corporation which violates its provisions, shall be punished by imprisonment not exceeding thirty days, and by fine not exceeding \$1,000, or either, at the discretion of the court. Moreover, an offending corporation will not be aided by Pennsylvania courts in enforcing contracts made in this state. This statute has worked no little hardship. The agent of a foreign corporation which has not duly registered may incur personal liability on contracts entered into by him on its behalf.

In the case of *Construction Co. v. Railway Co.* (1902), 204 Pa. 22, the construction company claimed over \$30,000 for labor and material furnished under a contract for certain railway work. This concern was chartered in New Jersey, and was registered in Pennsylvania about two months after the work on the railway had been completed. The Supreme Court held that it had no right to the aid of a Pennsylvania court in enforcing the contract. The construction company was engaged for six months on a railway line in Pennsylvania, and employed a large amount of its capital here. The fact that the company had registered afterwards did not help it. The purpose of the statute of 1874 is not accomplished by a registering of the corporation at the pleasure of its officers, or when it may be to its interest to appeal to our courts. The statute is for the protection of those with whom it does business or to whom it may incur liability by its wrongful acts, and nothing short of a registration before the making of the contract which it seeks to enforce can give it a right of action. The act of 1874 has been held not to cover isolated transactions between foreign corporations and citizens of this state. Thus, in the case of *Exposition of National Carriage Dealers' Association* (1902), 12 D. R. 10, it appears that a meeting of carriage dealers for the promotion of trade does not bring the Dealers' Association within the scope of the act.

The case of *Dryer Co. v. Bigler & Co.* (1890), 192 Pa. 466, shows that a foreign corporation which has no office or place of business in Pennsylvania, and no part of its capital invested here, need not comply with the act of 1874. The Dryer

Company sold Bigler & Co. machinery, which was shipped either directly from its Chicago factory or upon its orders given to other manufacturers. The court held that the Dryer Company was not brought within the statute of 1874 *merely because its agent came into this state*, and made contracts for the delivery of the machinery here. To hold otherwise would make the statute offend against the Constitution of the United States by imposing unlawful restrictions on interstate commerce.' A corporation of one state may send its agents to another to solicit orders for its goods, or contract for the sale thereof, without being embarrassed or obstructed by state requirements as to taking out licenses, filing certificates, establishing resident agencies, or like troublesome or expensive conditions. *Product Co. v. Philadelphia* (1906), 15 D. R. 587.

In *Hovey's Estate* (1901), 198 Pa. 385, it was held that a *foreign corporation which sells its goods to commission merchants*, and has no place of business in Pennsylvania, need not register. Accordingly, if a Pennsylvania commission merchant guarantees his sales, the unregistered foreign corporation which employs him may bring suit here either against him or against the purchaser. In the case of *Association v. Berlin* (1901), 201 Pa. 1, the Supreme Court reversed the Superior Court, and upheld a loan of money made to a Pennsylvanian by a New York company through a local agent without compliance with the act of 1874. The borrower's bond was secured by a mortgage on Pennsylvania real estate, but the contract of lending the money was, in the eye of the law, made in New York, where the association exercised its corporate functions. See also *Optical Co. v. Insurance Co.* (1904), 24 Super. 527, and *Holmes Co. v. Barnard* (1884), 15 W. N. C. 110.

A foreign corporation should be careful to obey the act of 1874 literally, for a defective compliance with its terms may be useless. From the case of *Manufacturing Co. v. Reilley* (1898), 187 Pa. 526, it appears that if a foreign corporation has filed a statement designating a place of business in one county, and subsequently removes to another

county, it is bound to file a new statement showing the new place of business. Where it has more than one branch store in the same county, and its various stores are separately organized and do business as independent concerns, it should file a statement designating all of its business houses, and its authorized agents therein, and each of said agents should keep a certificate for public inspection in each of said offices, respectively. *Wall Paper Co.'s Appeal* (1900), 15 Super. 407. When a foreign corporation seeks to enforce in a Pennsylvania court demands growing out of the transaction of business in this state, it should prove, as part of its case, that it obtained the right to do business here by complying with the act of April 22, 1874.

(C) *Domestication of foreign corporations.*

The act of June 9, 1881, provides that corporations formed under the laws of any other state and doing business within Pennsylvania may renounce their foreign charter, and become Pennsylvania corporations upon certain terms. These terms are almost the same as are prescribed for the formation of an entirely new company under the act of April 29, 1874. The same bonus must be paid as in the case of the original formation of a Pennsylvania company. The application must be sent to the Secretary of the Commonwealth, and advertised in the way marked out for the formation of a Pennsylvania company. The provision as to recording is also the same. Three of the stockholders must be citizens of Pennsylvania. The application must contain the following information: (1) The name of the corporation; (2) its purpose; (3) the place or places where its business is to be transacted; (4) the term for which it is to exist; (5) the names and residences of the stockholders, and the number of shares held by each; (6) the number of its directors, and the names and residences of those elected for the current year; (7) the amount of its capital stock, and the number and par value of the shares into which it is divided; (8) the legislation under which it was originally created; (9) its financial condition at the date of the certificate, showing capital stock paid in, funded debt, floating debt, estimated value of property and cash assets, if any.

The application must be accompanied by a certificate under the corporate seal showing the consent of a majority in interest of the corporation to the application for a charter, and the renunciation of its original foreign charter and of all privileges not enjoyed by corporations of its class under Pennsylvania laws. The certificate must be acknowledged by at least three of the directors before the Recorder of Deeds of the county where the chief operations of the corporation are to be carried on, or in which its principal office is situated. The said directors must also make and subscribe an oath or affirmation before the Recorder, to be indorsed on the certificate, that the statements contained therein are true. Ten per cent of the authorized capital should be paid into the treasury before the application is made.

A new name may be chosen by the corporation thus naturalized and domesticated in Pennsylvania. It still retains, however, all of the rights, privileges, powers, immunities, lands, property and other assets that it originally owned, except such as are inconsistent with its new charter. Moreover, all suits, claims, and demands of the corporation, in existence at the date of the new charter, may be sued on under the laws governing the said corporation prior to its new charter, as if no change had taken place.

BOOK THIRD

PERSONAL AND REAL PROPERTY

PART I

BAILMENTS, INCLUDING CONTRACTS FOR PLEDGING, HIRING AND TRANSPORT- ING PERSONAL PROPERTY

CHAPTER XXXV.

THE DEFINITION OF A BAILMENT AND VARIOUS FORMS THEREOF.

A bailment is defined as a delivery, by one party to another, of personal property which is to be held in accordance with the purpose of the transaction, and is to be returned or otherwise disposed of when that purpose is accomplished. Personal property is distinguished from real property. The latter is often called real estate or realty. Real property includes land and almost everything built or growing on or affixed to land, also certain interests in land, such as ground rents. Everything else is personal property, including live stock, cash, mortgages, bonds, and other evidences of debt.

In this third book we shall consider contracts affecting property and various kinds of property rights. These rights may be obtained in two ways: first, by original acquisition; second, by transfer. The first way includes the capture of property in war, the discovery of lost or abandoned property, whose owner does not claim it, or of property which never

had an owner, and the occupancy of unclaimed real estate. The first way also includes the acquisition of property by accession, as where your land yields crops or your brood mares give birth to issue. It also includes the original products of mental effort, which are secured as property rights by patent and copyright laws.

The second way by which title to property is obtained includes transfers which take place by act of law, as in the case of the purchase of a man's property which is sold by the sheriff in legal proceedings against him. Other transfers by act of law occur in the case of forfeiture of property for crime or other delinquency; and of bankruptcy which transfers the bankrupt's property to the representative appointed to distribute it among his creditors; and of intestacy, where a person dies without leaving a will, and his property is distributed among his relatives in accordance with the intestate law.

The second way by which property rights are obtained includes also *transfers by the act of a party who owns property*. A property owner may give his property away during his lifetime or may leave it by will upon his death, subject to the rights of his creditors and certain others. He may also transfer it by selling or by hiring, lending or pledging it, or by making some other disposition of it. The transfers mentioned in the preceding sentence are those which will occupy us almost exclusively throughout this third book.

If you are the sole and absolute owner of property, whether real or personal, and have possession of it, your property rights with respect to it are complete. There are numerous ways in which more than one person can have rights concerning the same property. As we saw in the second book, there may be many joint owners of a single tract of real estate or a single article of personalty. What concerns us in the chapters about bailments, however, is that the ownership may be in one party, while another may have either a right to the present use of it or may have a right to hold it as security till some claim of his shall be paid. This requires us to study not merely such transfers as pass the entire and absolute ownership of property from one person to another, but also those which

transfer certain property rights of an inferior degree. In the third part of this book we shall take up leases of realty, by which a tenant acquires possession but not ownership of the leased premises. In this first part of the book on property, we shall consider those transfers of personalty which are called bailments.

Suppose you own a watch, and pledge it with a pawnbroker. This is a bailment, for you do not transfer the ownership to him, but merely the possession, and the right to retain it until the loan is repaid, with interest and proper storage charges. If you leave it with a jeweler to be repaired, this is another form of bailment. Likewise, if you lend it or hire it to a friend, or hand it to him in order that he may hold it for you. Likewise, if you send it by messenger. In all these cases you are the bailor, the one who delivers the property. The pawnbroker, the jeweler, as well as your friend and the messenger are all bailees, the parties to whom the article of personalty is delivered. In these various transactions certain rights and obligations arise between bailor and bailee, also between the bailor and third parties, and between the bailee and third parties. The bailee is frequently an agent of the bailor, in a certain sense, but this subject should be kept distinct from agency. It will be interesting, however, to compare what is said here with the remarks concerning the agency relation at the beginning of the twentieth chapter. We shall consider in the following chapter the bailee's obligations towards the bailor and towards third parties. In chapter thirty-seven we shall take up the bailor's obligations towards the bailee and towards third parties, and in chapter thirty-eight the obligations of third parties towards the bailor and the bailee. Chapter thirty-nine will be devoted to the subject of the transportation of personal property. This is a special kind of bailment which introduces several peculiar rules, and is, therefore, treated separately.

CHAPTER XXXVI.

THE BAILEE'S DUTIES AND OBLIGATIONS.

A bailment transaction naturally puts the bailee under an immediate obligation towards the bailor, who has delivered the property for a certain purpose. Any obligations which the bailee may be under towards third parties are usually of comparatively slight importance. This chapter, therefore, will treat mainly of the bailee's obligations towards the bailor.

(A) Towards the bailor.

The amount of care which the bailor may require the bailee to exercise in taking charge of the former's property varies with the nature of the bailment. If the bailment is for the benefit of the bailor or of some person whom he represents, the bailee is responsible only for gross negligence. If it is for the benefit of both parties, he is bound to display ordinary care. If it is for the benefit of the bailee or of some party represented by him, he is liable for the slightest neglect. In the three following paragraphs we shall consider these three situations in the order named.

Bailment for the bailor's benefit.—In *Bank v. Graham* (1875), 79 Pa. 106, Graham sued the bank to recover the value of four United States bonds which had been left by her with the bank for safekeeping, and for which the bank had given her a receipt. Several years later they were stolen from the bank along with other valuables. The court held that she could win her suit only by proving that the bank had failed to exercise such care as even the most thoughtless men take of their own concerns. The bailee without reward is not bound to ordinary diligence, or to that care which every watchful person takes of his own goods, but only to such care as the most inattentive take. The thief who stole the bonds took also \$3,500 belonging to the bank which was in the same safe. The fact that the bailee has dealt with his own property and the bailor's in the same way may be shown as some evidence of care, as well as a test of the bailee's good faith. Even where

the president or teller of a bank, which acts as a bailee without hire of certain bonds, fraudulently pledges or steals the bailor's bonds, the bank is not liable, unless the bank management was grossly careless. *Scott v. Bank* (1873), 72 Pa. 471. *Bank v. Rex* (1879), 89 Pa. 308. In the case of *Tompkins v. Saltmarsh* (1826), 14 S. & R. 275, these principles were applied to the free carriage of a letter containing money. The messenger lost the letter, and was sued. He received the letter in the District of Columbia, and was to take it to Athens, in Bradford County, Pennsylvania. The court held that he was not bound to lay aside all other business and to take the direct road to Athens. He was answerable only for gross neglect, and was not bound to show that the letter had been stolen from him.

The case of *Rodgers v. Stophel* (1858), 32 Pa. 111, shows the measure of a wharfinger's liability where the bailment is *for the benefit of both parties*. Stophel deposited lumber on Rodgers' wharf, agreeing to pay for the use of the wharf. The lumber was stolen by a third party, and the court held that Rodgers was responsible for the loss if he did not display reasonable and ordinary care. It does not follow that every landowner, who permits another to store property upon his premises, is bound to watch the property, if he receives pay for the use of his land. A wharfinger, however, is expected to look after the safety of goods on his wharf. In the case of *Woodruff v. Painter & Eldridge* (1892), 150 Pa. 91, the bailees were sued for the value of a watch. The plaintiff had been trying on a suit of clothes in the bailees' store. He took off his watch, and the salesman suggested that he put it in a certain drawer, adding, "it will be safe, I guess." The watch disappeared. The jury decided that the bailees had been negligent. The question arose whether they were bound to exercise ordinary care as bailees for hire or only slight care as gratuitous bailees. The court held that they were bailees for hire, for they received their recompense in the profits of the clothing trade, of which the bailment was an incident. In the case of *Hunter v. Jacob Reed's Sons* (1899), 12 Super. 112, a customer was allowed to recover for money stolen from his clothes, which he had hung up in a dressing booth. He had

tried on a new pair of trousers, and was invited by the salesman into the next room where there was a mirror. When he returned to the dressing booth, he found a strange man there, and soon discovered that \$41 and a diamond ring had been taken from the pockets of his old trousers. He promptly notified the shopkeeper, who disclaimed responsibility and took no measures to recover the property, although Hunter pointed out the man whom he had found in the booth. The jury gave a verdict in favor of Hunter for \$41 and the value of the ring, but the court refused to allow a recovery for the stolen ring. It would be natural to expect that Hunter would carry money in his pockets, but the proper place for his ring was on his finger. When property is of an extraordinary kind or value, or is carried in an unusual way, the customer should put the storekeeper on his guard, so that the latter may have a chance to decline to accept the risk. Jacob Reed's Sons had placed a notice in the dressing booth, stating that they were not responsible for articles left there. Hunter swore that he did not see this, and there was no evidence that his attention was directed to it. The court said that the jurymen considered, perhaps, that the size and location of the notice were not sufficiently prominent to attract the attention of an ordinary man, or that it did not apply to Hunter at all. Hunter had not finished his use of the dressing booth, and the notice did not plainly state that the storekeepers were not responsible for articles deposited there by customers who had not finally "left" the booth, but were outside for a moment inspecting clothes. The case of *McFarland v. McClces* (1886), 17 W. N. C. 547, holds that a professional money-lender, who receives money for investment, is bound to exercise reasonable care and prudence.

In the case of *Todd v. Figley* (1838), 7 Watts 542, Figley sued Todd for the value of a mare, which he had lent Todd. The mare died as a result of being kicked by another horse. The court charged that as Todd, *the bailee, was the only person to be benefited* by the loan of the mare, he was bound to take extraordinary care of her, and became liable to pay Figley for any loss sustained even through slight negligence on Todd's part. Todd, perhaps, had not promised

expressly to take great care of the beast, but such an undertaking on his part was to be implied. The word "bailment" comes from the French word "bailler," meaning "to deliver." It is a delivery of goods in trust, upon a contract expressed or implied, that the trust shall be faithfully executed by the bailee.

Any improper use of the bailor's goods subjects the bailee to liability for resulting loss. In the case of *Persch v. Quiggle* (1868), 57 Pa. 247, Cordelia Quiggle sued Samuel Hepburn and others for the value of a certain stock certificate. Upon her departure for Europe, she had given this certificate, with a blank power of attorney, to Hepburn for safekeeping. Hepburn turned over the certificate and power of attorney to Persch, without Quiggle's knowledge or consent, and Persch pledged the stock to a bank. Both Persch and Hepburn were liable to Quiggle for these wrongful actions. Even if Hepburn was a bailee without hire, he had no right to use the property for his own purposes or to expose it needlessly. His action in loaning it was not for Quiggle's benefit, but showed that he was treating the bailor's stock as if it had been his own. In the case of *Smuller v. Canal Co.* (1860), 37 Pa. 68, it appeared that Smuller had received money from the company for the special purpose of paying the company's debt to Joseph Chamberlain. He paid most of this money to Chamberlain, but kept the rest on account of a debt due by the company to a firm of which he was a member. Usually, when a defendant is sued, he is permitted to set off, against any claim which may be made against him, a debt due by the plaintiff either to himself or to a firm of which he is a member, if his partners consent. In this case, however, it would have encouraged fraud to let a bailee receiving money for one specific purpose to convert it to his own use, or that of his firm, even though he or his firm had a just claim against the company. A bailee cannot refuse to return the property to the bailor on the plea that the latter has no title to it, unless a third party has given clear notice to the bailee of the bailor's lack of title, and warned the bailee against recognizing the bailor. Where the bailor knows exactly how the bailee is taking charge of the property, and makes no complaint, he cannot well object, if loss ensues after-

wards, that the bailee's methods were negligent. If any extraordinary cause of danger comes to the bailee's knowledge, he should increase his vigilance. For instance, if there is an epidemic of robberies in a certain town, the custodians of others' property should be especially diligent to prevent loss. As soon as a theft of the bailor's property is made known to the bailee, he should take prompt measures to recover it, and should usually give immediate notice to the bailor.

Where stock certificates are pledged to secure a loan of money, and the stock declines in value, the pledgee is not bound to sell it in order to save the owner from further loss. Where, however, the owner commands him to sell it, and the market price at the time is so high that the proceeds of a sale would repay the loan, the pledgee continues to hold the stock at his own risk. If it subsequently declines, he must bear the loss. See the case of *Peterson v. Safe Deposit Co.* (1885), 4 Walker 430. Where a promissory note or book account is assigned to a creditor as collateral security, he should use ordinary diligence to collect it.

A pledgee to whom shares of stock are given as collateral must always have them ready for redemption. He is not bound to return the identical certificates that were pledged to him, if he can prove that he continually kept control of the required number of shares, and was prepared to deliver them. See the case of *Stuart v. Bigler* (1881), 98 Pa. 80. If he receives dividends on the stock, he should be careful to give credit to the proper party, and keep his accounts in such shape that the amount due him by the pledgor, the owner, may be readily ascertained. If the pledgee exercises a right to sell the pledgor's property, he must give the latter credit for the price received.

The relation of the bailor and bailee is one of trust, and the former's rights are not extinguished by the passage of six years, as in the case of the outlawry of a debt. In the case of *Johnston v. Humphreys* (1826), 14 S. & R. 394, Johnston was sued to recover money given him in Philadelphia for transmission to Ireland. He had never forwarded the money, but defended on the ground that more than six years had

elapsed between the delivery of it to him and the commencement of suit. The court held that no lapse of time is a bar to a suit against a trustee. Thus, an executor or administrator of a dead man's estate cannot set up the statute of limitations against the rights of those interested in the estate. In the case of *Reynolds v. Cridge* (1890), 131 Pa. 189, it appeared that bonds had been left with a pledgee as collateral security for over six years, without either an offer by the pledgor to redeem them or a demand by the pledgee for payment of the debt secured. The court held that mere lapse of time is no bar to the pledgor's rights. If it appears that the pledgor intended to abandon the security, or if he is estopped by other circumstances, the situation is different. In *Morris's Appeal* (1871), 68 Pa. 16, the court refused to allow the First City Troop of Philadelphia to recover a document from the descendants of the captain who had commanded them during the Revolution. The document had been claimed in 1824 by this captain's son, who then had possession of it, and the City Troop acquiesced in his claim. Thirty years later the City Troop demanded the document from a grandson of the captain, and thirteen years after this sued his great-grandson for it. The court dismissed their suit, saying that if the document had been upon deposit or bailment before 1824, the relation ended at that time. The captain's son had clearly and openly denied the right of the City Troop, and had remained in exclusive adverse possession of the document with the Troop's full knowledge. Their long delay subsequent to 1824 was fatal. See also the case of *Wambold v. Hoover* (1885), 110 Pa. 9.

(B) *Towards third parties.*

A bailment does not place the bailee under any special obligation towards third parties. It goes without saying that he must not deceive them by pretending to be the absolute owner, and that he is liable to them for the consequences of such false pretenses. Towards the end of the tenth chapter on negotiable contracts, it was mentioned that the act of September 24, 1866, makes certain bills of lading and warehouse

receipts negotiable. In order to protect third parties to whom these documents may be transferred, the act prescribes severe penalties for a bailee who issues a false bill of lading or warehouse receipt. Furthermore, no warehouseman, wharfinger or other person who has issued such a receipt for goods stored may sell, encumber, ship, transfer, or in any manner remove beyond his immediate control any goods represented by the receipt, unless it is returned to him.

In considering the bailee's obligations towards the bailor, we saw that he is ordinarily bound to recognize the bailor only. He cannot, however, pervert this obligation and justify the closing of his eyes to the rights of third parties. In the case of *Hindmarch v. Hoffman* (1889), 127 Pa. 284, Hoffman, a bailee, was sued for money deposited with him by a thief. It had been stolen from Hindmarch, who notified Hoffman. After receiving the notice Hoffman had returned the money to the thief, but he was held liable to pay it over again to Hindmarch, the real owner. See also *Robinson v. Hodgson* (1873), 73 Pa. 202, and *Clowes v. Hughes* (1897), 3 Super. 561.

CHAPTER XXXVII.

THE BAILOR'S DUTIES AND OBLIGATIONS.

The bailor's duties and obligations extend towards the bailee and towards third parties. He owes most of them to the bailee, and the subject of his relation towards third parties does not call for lengthy treatment.

(A) *Towards the bailee.*

The chief obligation which the bailor owes to the bailee is that of compensating him for the value of his services. This obligation does not exist where the bailment is for the bailee's benefit, or in any other case where it is understood expressly or impliedly that the bailee is not to be paid. In most bailments, the bailee performs some service for the bailor, and his

compensation is either expressly agreed upon or implied from the nature of the relation. In the case of *Grove v. Barclay* (1884), 106 Pa. 155, Grove sued to recover for the use of a storage room. Barclay had occupied this room with his machinery for ten years before the suit was brought, and the court held that an implied contract arose to pay rent. Barclay had been ordered to remove the machinery at one time, but refused to do so, threatening to hold Grove liable if Grove removed it himself. As Barclay disregarded Grove's quit-notice, and Grove took no immediate measures to evict him, his occupancy of the premises continued as before, and he was bound to pay rent for the period after he had been notified to leave, as well as for the previous period. Likewise, if you take a tool to a machine shop, in order that it may be repaired, an implied contract arises whereby you are bound to pay for the repairs, if made in a workmanlike manner and according to your instructions. Likewise, if you send your horse to a livery stable, an implied contract springs up between you and the stablekeeper, obliging you to pay for the horse's food, shelter and care. Likewise, if you send your tailor a roll of cloth to be made into a suit of clothes. Where no sum has been agreed upon between the parties, the bailee may recover the fair and reasonable value of his services.

Not only does the bailee have a right to sue the bailor in cases where there is an express or an implied agreement to pay him, but he has also in most such cases a *right to retain the property of the bailor as security for the payment of his services in connection with it*. This right is called a lien, and it is implied by law in the case of most bailments. If, however, the bailee agrees to extend credit to the bailor, he cannot break his contract, and hold the goods after they should be returned to the bailor. In the case of *Lee v. Gould* (1864), 47 Pa. 398, it appeared that Gould had received hides which were to be tanned by him into sole leather, and to be returned within a reasonable time. His charges were to be paid after the return of the hides, and the court held that he had no lien. The case of *Mathias v. Sellers* (1878), 86 Pa. 486, was a suit against a cigar manufacturer to obtain possession of a lot of cigars.

The cigars had been made up from tobacco furnished by the plaintiffs. When suit was brought, the manufacturer's bill for work on the cigars amounted to over \$2,000. He had been allowed to sell some of them as agent for the plaintiffs, and the net amount due him was less than \$300. The court held that the plaintiffs, the owners of the cigars, should not have brought suit to obtain possession of them without paying or at least tendering to the manufacturer the amount of this net balance. Goods deposited with a tradesman or artisan for manufacture or repair are subject to a specific lien for work done on them. Thus, a dyer, who has dyed cloth delivered to him, is not bound to return it to his employer until paid for his services. Neither is a ship carpenter bound to restore the ship which he has repaired; nor a jeweler the gem which he has set, or the seal which he has engraved. As the manufacturer in the above mentioned case of *Mathias v. Sellers* had been allowed to sell some of the cigars, he was entitled to retain the proceeds towards payment of his claim. If, however, he had delivered a previous lot of cigars to the owners for whom he had made them up, he would have abandoned a right to a lien on those cigars, and he could not hold the subsequent lot as security for the payment of his charges for the previous work. The bailee's lien is *specific*, which means that he may retain a particular article belonging to the bailor as security only for his charges concerning that article. Even if a bailee has previously done work on the same article, and has returned it to the bailor, who redelivers it to him later for other work to be done on it, the bailee may hold it the second time only to secure payment for his second job. Where, however, several articles are delivered to him *at the same time under a single contract* of bailment he may hold them all as security for the payment of his charges on any article. The bailor cannot obtain the right to a delivery of one of such articles merely by paying the bailee's charges for work on that article alone. Neither can the bailor obtain one of the articles by proving that the others, of which he is willing to have the bailee retain control, are of sufficient value to secure the bailee. See the cases of *Yearsley v. Gray* (1891),

140 Pa. 238; *Hensel v. Noble* (1880), 95 Pa. 345, and *Young v. Kimball* (1854), 23 Pa. 193. Sometimes a special agreement is made between the parties, whereby the bailee is allowed to hold any property belonging to the bailor, which may be in his possession, as security for all moneys due him by the bailor. This idea is embodied in the form of a collateral security note given in the twenty-seventh chapter. Considerable is said about the rights of a pledgee of corporate stock in that chapter, which may be read in connection with the present topic.

The bailee must have exclusive possession of the article, in order to assert a lien against it. In the case of *Fitzgerald v. Elliott* (1894), 162 Pa. 118, a lien on certain logs was claimed by Fitzgerald, who had been employed to cut them and place them in a certain pond. The logs were not on his land, and he had not an independent possession of them. The pond belonged to his employer, and he was no more a bailee than a coal miner who handles coal in his employer's mine. A laborer employed to dig ore, for instance, is no bailee, and has no lien on the ore for his wages. Laborers engaged in lumbering work receive a certain preference out of the proceeds of sheriff's sales and certain other public or official sales under the act of May 7, 1891, but they have no lien as bailees upon the lumber.

The finder of lost property has no lien on it for the trouble and expense incurred in taking charge of it, for the right to a lien flows from the bailor's agreement that the bailee shall have possession of the property. Likewise, if the bailee, without express or implied authority from the bailor, turns the property over to a third party, the latter has no lien on it. Thus, in the case of *Meyers v. Bratespiece* (1896), 174 Pa. 119, a bailee, who received cloth which was to be made up into coats, delivered some of it to Bratespiece, who agreed to do the required work. Meyers, the bailor, had not authorized this delivery, and sued Bratespiece in replevin to recover the coats which the latter had made. The bailee had absconded, after collecting from Meyers some of the money due for the coats. The court decided against Bratespiece, for in order to

charge a chattel with a bailee's lien, the labor for which the lien is claimed must have been done by the claimant at the owner's request, or under circumstances from which his assent can be reasonably implied. Ordinarily, therefore, a bailee cannot appoint a sub-bailee, just as an agent cannot appoint a sub-agent.

Similarly, if the holder of another's property makes unauthorized repairs to it, he cannot claim a lien on account of the services which he voluntarily rendered. If, however, the bailee has been put in possession of property by the bailor, and it becomes necessary to take measures to preserve the property, the bailee has a lien for the resulting expenses. In the case of *Hoover v. Epler* (1866), 52 Pa. 522, Epler claimed a lien upon Hoover's stallion for the expenses of keeping him and having him shod. When Epler had received the stallion probably nothing had been said about shoeing him, but fidelity to Epler's employer required that the animal should be shod. Therefore, when Epler paid the blacksmith's bill he was not in the position of one who voluntarily thrusts services upon another. Of course, Epler could not have claimed a lien for the horseshoeing bill, and refused to deliver the stallion to Hoover, until paid the amount thereof, if he had not really paid the blacksmith.

A number of statutes have been passed to fix precisely the relative rights of the bailor and the bailee in certain cases. The act of December 14, 1863, provides that whenever commission merchants, factors and all common carriers, or other persons, shall have a lien under existing laws upon any goods or other property, on account of the expense of carriage, storage, or labor bestowed on such goods or other property, if the owner or consignee shall fail or neglect to pay the amount of such charges within sixty days after demand thereof, made personally upon such owner or consignee, it may be lawful for the holder of any such lien to expose the goods or other property to sale at public auction, and to sell the same, or so much thereof as shall be sufficient to pay the lien along with costs of sale and advertising. Notice of the sale, together with the name of the person or persons to whom

the goods shall have been consigned, must be previously published for three successive weeks in a newspaper published in the county, and by six written or printed handbills put up in the most public and conspicuous places in the vicinity of the depot where the property may be. If the goods are perishable, or the residences of the owner and consignee are unknown, the lienholder may present a petition under oath to any of the judges of the Courts of Common Pleas, setting forth the facts. 'The judge who is applied to may give a signed order, authorizing the sale of the property upon such terms, as to the giving of notice, as the nature of the case may permit. In the case of perishable property, the proceedings may also be taken before a justice of the peace.

Since the passage of the act of 1863, a bailee of property who has a lien upon it may transfer possession of the property to a third person, and this third person may exercise the same right of lien as the bailee himself. See *Rodgers v. Grothe* (1868), 58 Pa. 414. The act of May 21, 1857, allows factors and other agents for parties outside the state to contract for 7 per cent interest in certain cases. The act of April 7, 1807, gives keepers of inns and livery stables a special lien on horses stabled by them. The act of May 7, 1855, gives innkeepers a special lien on the goods of boarders.

The Factors' Act of April 14, 1834, is as follows:

1. Whenever any person entrusted with merchandise, and having authority to sell or consign the same, shall ship or otherwise transmit the same to any other person, such other person shall have a lien thereon: First, for any money advanced or negotiable security given by him on the faith of such consignment, to or for the use of the person in whose name such merchandise was shipped or transmitted; second, for any money or negotiable security received for the use of such consignee, by the person in whose name such merchandise was shipped or transmitted.

2. Such lien shall not exist for any of the purposes aforesaid, if such consignee shall have notice by the bill of lading or otherwise, before the time of such advance or receipt, that the person in whose name such merchandise was shipped or transmitted is not the actual owner thereof.

3. Whenever any consignee or factor, having possession of merchandise, with authority to sell the same, or having possession of any bill of lading, permit, certificate, receipt or order, for the delivery of merchandise, with the like authority, shall deposit or pledge such merchandise, or any part thereof, with any other person, as a security for any money advanced or negotiable instrument given by him on the faith thereof, such other person shall acquire by virtue of such contract the same interest in and authority over the said merchandise as he would have acquired thereby if such consignee or factor had been the actual owner thereof: Provided, That such person shall not have notice, by such document or otherwise, before the time of such advance or receipt, that the holder of such merchandise or document is not the actual owner of such merchandise.

4. If any person shall accept or take such merchandise or document from any such consignee or factor, in deposit or pledge for any debt or demand previously due by or existing against such consignee or factor, and without notice as aforesaid, and if any person shall accept or take such merchandise or document from any such consignee or factor in deposit or pledge, with notice or knowledge that the person making such deposit or pledge is a consignee or factor only, in every such case the person accepting or taking such merchandise or document in deposit or pledge shall acquire the same right and interest in such merchandise as was possessed or could have been enforced by such consignee or factor against his principal at the time of making such deposit or pledge, and no further or other right or interest.

5. Nothing in this act contained shall be construed or taken: (I) To affect any lien which a consignee or factor may possess at law, for the expenses and charges attending the shipment or transmission and care of merchandise consigned, or otherwise entrusted to him. (II) Nor to prevent the actual owner of merchandise from recovering the same from such consignee or factor, before the same shall have been deposited or pledged as aforesaid, or from the assignees or trustees of such consignee or factor in the event of his insol-

vency. (III) Nor to prevent such owner from recovering any merchandise so as aforesaid deposited or pledged, upon tender of the money, or of restoration of any negotiable instrument so advanced, or given to such consignee or factor, and upon tender of such further sum of money, or of restoration of such other negotiable instrument, if any, as may have been advanced or given by such consignee or factor to such owner, or on tender of a sum of money equal to the amount of such instrument. (IV) Nor to prevent such owner from recovering, from the person accepting or taking such merchandise in deposit or pledge, any balance or sum of money remaining in his hands as the produce of the sale of such merchandise, after deducting thereout the amount of money or the negotiable instrument so advanced or given upon the security thereof, as aforesaid.

(B) *Towards third parties.*

Ordinarily the bailor is not brought into legal relations with third persons through the bailment contract. The bailee is usually not the bailor's agent in the sense in which agency was considered at the beginning of the second book. *He is usually rather an independent contractor dealing with the bailor for himself than the bailor's representative in dealings with third persons.* In the case of *Bard v. Yohn* (1856), 26 Pa. 482, Yohn brought suit against a farmer for injuries received by him from one of the farmer's horses. The farmer's son had used his father's team to drive some people to Reading, in order that they might attend a fair. He took the team without his father's permission, and kept for himself the money which he earned. While the horses were being fed on a street in Reading, one of them kicked Yohn as he was driving by. Yohn alleged that his injuries were due to the negligent manner in which the horses had been fastened. The court held that the father would not have been responsible even if he had permitted his son to take the horses to Reading. If one hires out a horse to be used solely for the purpose of the man who takes it, the owner is in no wise responsible for the negligent manner in which the horse may be used. The

fact that the son worked on his father's farm did not create the relationship of principal and agent in the affair at Reading. The son alone was responsible for his own negligence.

In the case of *Rossell v. Cotton* (1858), 31 Pa. 525, Rossell was sued for damages caused by his cattle, which broke into Cotton's wheat field, and destroyed his wheat. At the time of the injuries the cattle were in charge of A. M. Hill, a bailee, who had made a contract with the owner for grazing them. Rossell was held to be free from responsibility for Hill's negligence.

In the case of *McColligan v. Penna. R. R. Co.* (1906), 214 Pa. 229, the company was sued for injuries caused by the negligence of a cab-driver. The cab had been leased by the company for a certain daily sum, and subject to its regulations. The driver was obliged to change his horse at certain intervals, wear a uniform, abstain from intoxicants and charge rates fixed by the company. It was held that the company did not control the driver in the way that a principal controls an agent, but had merely leased him a cab subject to certain conditions, and was not liable for his negligence.

The case last cited shows the advantage which may be gained by having your legal relation with one who takes charge of your property that of bailor and bailee, rather than that of principal and agent. Contracts are frequently drawn up with this object in view, so as to relieve the owner of property from responsibility for damages occasioned to third parties in the handling of it. When a building is about to be put up, the owner will be responsible for injuries negligently caused by those erecting it, if they are his agents. Accordingly, it is important to have the contract with the persons who are to build it so drawn up as to make them independent contractors. Usually a builder is an independent contractor, but it may be otherwise where the owner buys the materials himself and takes direct charge of the work, unless the contract is skilfully prepared.

In the following chapter we shall consider the rights of the bailor when the bailee fraudulently pledges or sells the bailor's property to a third party.

CHAPTER XXXVIII.

DUTIES AND OBLIGATIONS OF THIRD PARTIES.

As appears from the preceding chapter, a bailment contract does not usually bring the parties into immediate relations with third persons. Many agency contracts are made with the sole intention of bringing the principal into contracts with third parties through the medium of the agent. Most bailments, however, contemplate only a relation between the bailor and the bailee respecting the former's property. The bailee is not so much an agent as an independent principal, contracting for himself.

(A) Towards the bailor.

Third parties are bound to respect the bailor's rights. In the preceding chapter we saw that a bailee who has a lien on the property may usually transfer possession to a third party, and assign his own right of lien at the same time. The third party will then stand towards the bailor in the same position that was formerly occupied by the bailee. Generally, a third party's rights do not rise higher than those of the bailee who has transferred possession of the bailor's property to him.

In the case of *Quinn v. Davis* (1875), 78 Pa. 15, Davis sued to recover a piano, which he had deposited for storage with William Kirby. Kirby fraudulently put it up at an auction sale, where it was sold under Kirby's direction to Quinn, who paid for it in good faith. Kirby was a dealer in second-hand furniture, and Quinn contended that the storing of a piano with such a dealer was likely to help mislead innocent third parties as to the ownership. Kirby was not exclusively a dealer in goods. He also took goods on storage, and the court held that there was nothing in Davis's conduct, when he left the piano with Kirby, that was unlawful, negligent or imprudent. Quinn acquired no title at the auction sale, for Kirby had none himself. Even if the sheriff had seized the

property under the supposition that Kirby owned it, and sold it at an official sale, no title would have passed to the purchaser. *Crist v. Klever* (1875), 79 Pa. 290. In the case of *Rowe v. Sharp* (1865), 51 Pa. 26, Sharp sued to recover two billiard tables which he had hired to Charles A. Goff. Goff had been arrested in another transaction, and had delivered the tables to Rowe, who went bail for him, as security. The court held that Goff, the bailee, could not legally pledge the tables or make any similar contract respecting them without Sharp's consent. Sharp had agreed to sell the tables to Goff at a future date, but when Goff delivered them to Rowe they had not become Goff's property, and were still held by him as Sharp's property under an instalment lease. The distinction between a bailment of this kind and a sale will be treated at length in the fortieth chapter.

A bailor, who learns that his bailee is about to sell or pledge his property to innocent third parties, should promptly make his ownership known. In the case of *Greenhoe v. College* (1891), 144 Pa. 131, certain bailors sued a third party for the value of some machinery. The machinery had been delivered to the bailee, and afterwards sold at sheriff's sale as the bailee's property. The bailors had notice of this sale, but made no claim for the property until nearly two years afterwards. It was held on the well known principle of estoppel that they could not assert their rights, for they had helped to mislead the purchaser of the machinery into thinking that a good title would be passed by the sale. They should have publicly announced before the sale that they intended to claim the machinery, and thus warned off innocent third parties.

(B) *Towards the bailee.*

The bailee is not the owner of the property bailed to him, but he has the right of possession. This right of possession enables him to bring suit against a third party who maliciously or negligently injures the property while it is in the bailee's charge. He may recover not only the damages which he suffers by reason of being deprived of the full use of the

article, but also for all injuries caused to the property. Where the damages are recovered for a complete destruction of the property, the bailee should ordinarily hand them over to the bailor, or such a part of them as may be justly proportioned to the bailor's interest in the property. Where the property is wrongfully removed by a third party from the possession of the bailee, the latter may maintain a suit in his own name against the offender.

The bailee who lends money on the security of the bailor's property should remember that he ought to receive and retain possession of it. If the bailor is permitted to regain possession, and afterwards sells the property to a third person, the latter acquires a good title as against the bailee. A creditor or an innocent purchaser is not affected by a "chattel mortgage" in Pennsylvania, except as mentioned later. In some states the owner of personalty may mortgage it, while yet keeping it in his possession, and third persons are bound by the terms of the mortgage, if the requirements as to recording and other matters are properly fulfilled. Although a *chattel mortgage* generally has little value in this state, a *pledge* protects the pledgee if he gains exclusive *possession* of the property bailed to him. A third person who buys from the owner property which has been pledged or otherwise bailed, should take notice that the bailee has possession. While the bailee retains control of the property, he may assert any lien that he has upon it, not only against the owner but also against a third party who buys from the owner.

The law of Pennsylvania wisely refuses to recognize secret liens upon personal property. A bailee, therefore, should be careful not to part with possession of the bailor's property if he wants to protect himself. If he is asked about the ownership of it by a third person, who is about to purchase it from the bailor, the bailee should mention the fact that he has a claim on it, where it is pledged to him, or where he is holding it to secure a lien for services in connection with the property. If he misleads a third party into thinking that he holds it merely as the bailor's agent, he may be estopped from asserting his lien.

There are a few kinds of chattel mortgages which are valid in Pennsylvania. The act of April 5, 1853, permits mining rights in Schuylkill County to be mortgaged. The mortgage must be recorded within five days after it is executed in the Recorder of Deeds' office in that county. The act of May 20, 1891, provides that all iron ore mined and prepared for use, pig iron, blooms and rolled or hammered iron in sheets, bars or plates, iron and steel nails, steel ingots and billets, rolled or hammered steel in sheets, bars or plates, and all boilers, engines, oil, gas and artesian well supplies, and all steel or iron castings of every description not in place, all petroleum or coal oil, crude or refined, in tanks, barrels, reservoirs or other receptacle in bulk, all roofing and manufactured slate, as well as all slate quarried to be used for roofing or manufactured for other uses, asphaltum blocks, including all materials used in the manufacture thereof, all manufactured cement in barrels, bags or bins, including all materials on hand used in the manufacture thereof, may be mortgaged for any sum not less than \$100, by an instrument in writing, signed by the owner thereof, or by his agent, duly authorized and constituted, and duly acknowledged before some person authorized to take acknowledgments of deeds.

The act of April 28, 1887, supplies the following form for chattel mortgages of the articles just named. This form should be closely followed, but the parties may add any terms which are not inconsistent with the rest of the mortgage:

TO ALL WHOM THESE PRESENTS SHALL COME, GREETING: Know ye thatindebted unto in the sum ofdollars and cents, being for, now for securing the payment of the said debt and the interest from the date hereof to the said do hereby sell, assign and transfer to the said all the goods, chattels and property described in the following schedule, namely: Said property now being and remaining in the possession of.....: Provided always, And this mortgage is on the express condition, that if the said shall pay to the said the sum of with interest, as follows, namely: which said sum and interest the said hereby covenant to pay, then this transfer to be void and of no effect, but in case of non-payment of the said sum, at the time or times above mentioned, together with interest, then the said may give to the said

..... or to the person in possession of the property claiming the same, written notice as required by lawintention to foreclose this mortgage for breach of the condition thereof, and, if the said sum is not then paid, the said shall have full power and authority to enter upon the premises of the said party of the first part, or any other place or places where the goods and chattels aforesaid may be, to take possession of said property to sell the same according to law, and the avails, after deducting all expenses of the sale and keeping of the said property, to apply in payment of the above debt; if from any cause said property shall fail to satisfy said debt, interest, costs and charges, the said covenant and agree to pay the deficiency In witness whereof, has hereunto set hand and seal, the day of in the year of our Lord one thousand nine hundred and

Sealed and delivered in the presence of

.....

.....(Seal)

Such a chattel mortgage shall, except between the parties thereto, take effect and be valid only from the time that it is recorded in the office of the Recorder of Deeds of the county where the chattels actually are at the time the mortgage is executed. In case of more than one mortgage on the same chattels, the first to be recorded has preference, and must be paid first out of the proceeds of the sale of the chattels. A chattel mortgage may be assigned or released by a written instrument, signed by the mortgagee or his duly constituted agent, and recorded in the same office as the original mortgage. Such assignment or release is, except as between the parties thereto, valid only from the time of recording. Such a mortgage is not valid longer than three months after its maturity, unless a written statement signed by the mortgagee, or his duly constituted agent, and acknowledged, is recorded in the Recorder of Deeds' office, and specifies the amount due on such mortgage. This statement must be filed within three months from the maturity of the mortgage, which thereby continues valid for a further period of one year from maturity. The act of April 28, 1887, provides, furthermore, for the foreclosure of the mortgage and for other matters in connection with it.

The act of May 13, 1889, provides that a person who has conveyed or leased coal lands or other mineral lands, and who

has reserved a rental or royalty for his own benefit, may mortgage the rental or royalty. The mortgage should be recorded. The act of April 27, 1855, together with that of May 13, 1876, provides for the mortgaging by a lessee, who has leased for a term of years any colliery, mining land, manufactory or other premises, of his lease, with all buildings, fixtures and machinery on the premises belonging to him, the lessee. Such a mortgage is not allowed to interfere with the landlord's claim for rent, which has priority. The mortgage must be acknowledged and put on record in the county where the leased premises are located, along with the lease.

The act of June 12, 1878, allows a railroad company to mortgage its locomotives, cars and other personal property used to operate its road. Such mortgages may cover property subsequently acquired. *R. R. Co. v. Woolpper* (1870), 64 Pa. 366. Seven per cent interest may be charged on certain railroad bonds.

CHAPTER XXXIX.

TRANSPORTATION OF PERSONAL PROPERTY.

We now come to the subject of transportation of personal property. Our main topic will be the carriage of goods by a common carrier. Incidentally we shall briefly discuss the law relating to personal baggage of passengers on railroad trains. There are thousands of different methods by which property may be transported from one place to another by a bailee. Where the bailee is not a common carrier, his liability is to be determined according to the rules studied in Chapter XXXVI. The bulk of the transportation business is, however, in the hands of common carriers, who are subject to greater liability than the ordinary bailee: hence the necessity of treating this topic separately.

(A) *Who is a common carrier of goods.*

A common carrier is defined to be "one who holds himself out to the public to carry for hire from place to place."

Though the number of occasions on which an alleged common carrier has been employed in carrying may be evidence of the character of a common carrier, the law has fixed no number of instances which shall stamp him with the character. If he holds himself out to the public to carry for hire he is a common carrier as much in his first trip as in his second, third or fourth.

The distinction between a private and a common carrier is that a private carrier does not pursue the business of carriage as his usual occupation, while a common carrier undertakes the carriage of goods as a business and as a professed occupation.

In *Beckman v. Shouse* (1835), 5 Rawle 179, the court said "a private person may contract with another for the carriage of his goods and incur no responsibility beyond that of any ordinary bailee for hire, that is to say, the responsibility of ordinary diligence. But here the defendants pursued the business as a public employment, and undertook to carry goods for persons generally. They held themselves out as ready to engage in the transportation of goods for hire, as a business, and not as a mere casual occupation."

We generally think of railroads and express companies when we speak of common carriers, and it is no doubt true that they do the bulk of the business of carriage of goods. However, private parties may be common carriers. A ferryman is liable as a common carrier.

Boatmen of every description, upon rivers, seas or other bodies of water, come within the description of common carriers, if they engage in the business of carrying or transporting the goods of all persons that may employ them. The owners of vehicles of every kind, such as stages, coaches, cabs and street cars, who make it a business to carry for hire the goods of such as employ them, come within the definition of common carriers and are held liable as such. Many owners of vehicles whose principal business is to carry passengers, carry light baggage incidentally. When they carry goods for hire, they are common carriers as to such goods.

A pipe line company engaged in the business of transporting and storing oil for the public in pipe lines and tanks,

is a common carrier. The owners of a tow boat are not liable as common carriers for the safety of the boats which they undertake to tow or their contents.

A sleeping car company is not a common carrier. See *Pfaelzer v. Pullman Company* (1877), 4 W. N. C. 240. A passenger on a Pullman car lost some of his valuables on the car. The porter denied all knowledge of the occurrence, and the car was searched, but without any success. In a suit against the Pullman Company, the plaintiff contended that it should be held liable as a common carrier; but the court said that the contract of carriage was with the railroad company, and the effect of the contract with the sleeping car company was merely to give the plaintiff the privilege of sleeping in the car. The plaintiff was non-suited, for he failed to prove that the Pullman Company had been negligent, and proof of actual negligence is necessary in such cases where the carrier is not a "common" carrier.

(B) *Duty to receive and carry.*

A common carrier is bound to receive goods tendered to it by any person, provided they are goods of such a character as the carrier ordinarily carries, and provided they are properly packed. The shipper must tender the charges on the goods in advance if he wants to force an unwilling common carrier to transport them. No carrier can be required to take every kind of goods offered to him, if he cannot well adapt his means of conveyance to all kinds. The customs of the business and the manner of the carrier in conducting it, must always be taken into consideration in determining what are the goods which he is bound to accept for carriage. He can only be required to take what it can fairly be said he held himself out to the public as ready to carry. Ordinarily, a railroad company cannot be compelled to carry dogs, where it does not hold itself out as ready to do so.

(C) *Delivery to carrier.*

What amounts to delivery.—The carrier is not responsible for the goods until they have been delivered to him and

he has accepted them. The goods must be delivered to the carrier himself or to his authorized agent. The mere leaving of them in a place where the carrier will probably come and get them is not a delivery to the carrier, unless the goods are left in charge of an agent of the carrier. It is not a delivery for the shipper of the goods to load them into the carrier's conveyance without his knowledge. There must be a complete delivery into the actual custody of the carrier or his agent. Goods stored along the line awaiting shipment, where the owner is to load them when he can get the necessary cars, are not completely delivered to the carrier until they are so loaded and ready for shipment. The shipper must be careful to make a complete, actual delivery of his goods to the carrier in order that the latter's liability for the goods may attach. Goods should be delivered to the carrier at a customary place and during the usual business hours.

In *Spofford v. Pennsylvania R. R. Co.* (1899), 11 Super. 97, a shipper delivered goods about seven o'clock in the evening, when the carrier's warehouse was closed and locked for the night. He opened the door and put the goods in, there being no one in charge of the warehouse to receive the goods. In a suit against the carrier for the loss of the goods, it was held that there had never been a complete delivery to the company, and the latter was therefore not liable as a common carrier.

Delivery to connecting carriers.—Where a shipper delivers goods to a carrier, and the latter contracts only for himself, the contract being to deliver at the termination of his own route, to another carrier, he acts only as the shipper's agent in making the delivery to the connecting carrier. In such case, all the carrier is bound to do is to deliver the goods in proper condition to the connecting carrier. Where carriers agree to be liable only on their own lines, and to make delivery to connecting lines, they are forwarders only, beyond their own lines; and forwarders (unlike common carriers) are not insurers; that is to say, they are liable only for negligence. A carrier is not bound to accept goods for carriage beyond his

own lines. He may contract to carry to a point beyond the terminus of his own line so as to become liable for the delivery at such a point. If he does make such a contract, all the connecting carriers become his agents, and he is liable for their defaults. But there must be some positive contract, either express or implied, to extend the liability of a carrier beyond his own lines. If a shipper desires to send goods beyond the line of the carrier to whom he makes delivery, he cannot hold the first carrier liable for trouble occurring after the goods have been turned over to a connecting carrier, unless the first one expressly assumes this liability. Ordinarily a carrier will not do this, and he cannot be compelled to do it. It is said that, "a connecting carrier is one whose route, not being the first one, lies somewhere between the point of shipment and the point of destination." The carrier is bound to deliver to the connecting carrier to which it agrees to make delivery. If it delivers to some other carrier, and the goods are subsequently lost, it is liable to the owner of them.

In *Eckert v. Penna. R. R. Co.* (1905), 211 Pa. 267, it was held that where a railroad company takes horses for transportation beyond its own line, it assumes the duty of not only carrying the horses to the terminus of its road, but also of delivering them at that point to the connecting carrier in a car properly constructed and suitable to the purpose of transporting them to their final destination. If the carrier transfers horses to a car unsuitable to their safe carriage and they are thereby injured, the carrier is liable for the loss, and the fact that the person employed by the shipper to accompany the stock was present when the horses were transferred to the unfit car, and assisted in making the change, does not relieve the carrier from liability.

(D) Bills of lading.

The liability of the common carrier is created in large measure by the law and does not rest entirely upon contract. His liability for the goods attaches as soon as delivery of them has been made to him and accepted by him. As soon as

delivery is made and nothing remains for the shipper to do in the matter of forwarding them, the goods being intended for present carriage, the carrier is liable for the safety of the goods; hence no writing of any kind is required to make him liable as an insurer. However, a bill of lading is usually issued to the shipper. It is more than a receipt for the goods; it is also a contract for carriage. If the carrier is sued for the goods mentioned in the bill of lading he may show that it was given by mistake, and that the goods were never received by him, unless the bill has been transferred to an innocent holder for value. *Brooke v. R. R. Co.* (1885), 108 Pa. 529. The carrier may limit the rights even of innocent holders for value by issuing bills of lading marked "not negotiable." The bill of lading is frequently good evidence, however, not only of the quantity and kind of goods received, but also of their condition. So far as the bill of lading is a mere *receipt*, it may usually be contradicted by verbal evidence, except when in the hands of an innocent holder for value. So far as the carriage of goods, after they have been once received, is concerned, the bill of lading is a *contract*. It is subject to the rules relating to other contracts; and, therefore, when the carrier wishes to contradict by verbal evidence a term of the bill of lading which states, for instance, that the goods were to be delivered elsewhere than at the destination named in it, he cannot do so unless he can show that there was fraud or imposition on him in the affair, or a vital, mutual mistake.

The act of September 24, 1866, makes bills of lading negotiable by indorsement and delivery, but the purchaser of a bill of lading, having reason to believe that his vendor was not the owner of the bill, or that it was held to secure the payment of an outstanding draft, is not a *bona fide* purchaser, and is not entitled to hold merchandise covered by the bill against its true owner. Read what is said on this subject in Chapter X. For a case illustrating the negotiability of bills of lading, see *Hieskell v. Farmers' Bank* (1879), 89 Pa. 155. The carrier should not deliver goods except upon presentation of the bill of lading.

(E) *Duty to carry safely and to furnish facilities; discrimination.*

In general.—Having received the goods, the carrier is responsible for their safety. The general rule is that a common carrier is an insurer against loss or injury occurring in any way except by the act of God or the public enemy. It is usual for a carrier to limit his responsibility by contract so far as he can legally do so. The law permits this so far as such restriction of liability is not unreasonable or against public policy. In Pennsylvania a carrier cannot by contract escape liability for his negligence. No matter what contract he makes in an effort to restrict his liability, he is at least bound to take ordinary care of goods entrusted to him as carrier. The carrier is bound to provide places for the safe custody of the goods, and also persons to take care of such articles as are committed to the carrier's charge. Where the loss is caused by some act of the shipper or by the inherent nature of the goods, the carrier is not liable.

The most common cases in which the shipper of the goods is responsible for the loss are those in which he fraudulently misrepresents the character of the goods at the time he offers them for shipment. As a result of such deception the carrier does not perhaps give the goods the care and attention which he would have given them if he had known just what they were. It is a fraud upon the carrier, not only expressly to misrepresent the character and value of the goods, but also to do so by silence, where there is nothing to give the carrier notice as to the character and value of the goods. The carrier is not liable for a loss where the owner of the goods meddles with them while they are in the carrier's care. For instance, where the owner of live stock accompanies it upon a journey and insists that a car window be kept open, if the live stock escapes thereby and is killed, the carrier is not liable.

Duty of carrier to furnish facilities.—The carrier is bound to furnish reasonable facilities and appliances for the carriage of goods. He is bound to be ready to carry as great a quantity of goods as may be ordinarily expected to be offered for trans-

portation on his line. The vehicles must be safe and suitable for the business of carriage. He must do his best to carry the goods without undue delay.

In *Ritz v. Pa. R. R. Co.* (1858), 3 Phila. 82, it appeared that the plaintiff's sheep had been injured in transportation. In a suit against the company, the plaintiff claimed that the injuries resulted from the inadequacy of the cars. The carrier answered that the plaintiff loaded the sheep himself and that the carrier had nothing to do with it; but the plaintiff was allowed to recover.

In the case of perishable goods, the carrier is not liable for their decay, provided he uses reasonable means to preserve them, and is not guilty of undue delay in transportation. It is held in *Davenport Co. v. Pa. R. R. Co.* (1896), 173 Pa. 399, that a carrier is not bound to forward perishable goods in any special kind of car, unless he positively agrees to do so, or unless the usages of the business require it.

Discrimination in freight charges not lawful.—The Constitution of Pennsylvania provides that "no undue or unreasonable discrimination shall be made in charges for or in facilities for transportation of freight or passengers within the state or coming from or going to another state."

The act of June 4, 1883, provides that "no railroad company or other common carrier engaged in the transportation of property shall charge, demand or receive from any person, company or corporation for the transportation of property or for any other services, a greater sum than it shall charge or receive from any other person, company or corporation for like services, from the same place, upon like conditions and under similar circumstances; and all concessions, rates and drawbacks shall be allowed to all persons, companies or corporations alike, for such transportation and services, upon like conditions, under similar circumstances and during the same period of time. Nor shall any such railroad company or common carrier make any undue or unreasonable discrimination between individuals, or between individuals and transportation companies, or the furnishing of facilities for transportation. Any violation of this provision shall make the

offending company or common carrier liable to the party injured for damages treble the amount of injury suffered."

(F) *Custody and control of goods, and rights in them.*

In general.—In addition to the carrier's right to compensation for carrying goods (which we will treat later) the law gives him other rights in respect to goods. He has certain rights against the shipper, and he has rights against any person who may unlawfully interfere with him or the goods in his charge while he remains responsible for their safety. Being responsible for the safety of goods entrusted to him, he has a right to insure them to their full value. He has no right to sell the goods (except under a statute hereinafter mentioned), unless some extraordinary necessity arises and sale is required in order to save the goods. Such an emergency is apt to arise in the case of perishable goods. Where the carrier delivers goods to the consignee in the carrier's cars, a reasonable charge may be made for the use of the cars if the consignee keeps them longer than is proper. See *R. R. Co. v. Steel Co.* (1902), 201 Pa. 624.

Compensation of carrier.—The carrier is entitled to a reasonable compensation for the transportation of goods. He is entitled to demand this in advance, and to refuse to accept goods unless prepaid. If he does not demand prepayment he may claim his freight after he has carried the goods and is ready to deliver them. Where the carrier brings suit for the freight, the defendant is entitled to a set-off for any loss or damage to the goods for which the carrier is liable. Where a carrier does not require prepayment of charges, he has a right to retain possession of them at the point of destination, until the charges are paid or tendered. The whole amount of the freight is a lien upon every part of the goods, and if a part of the goods has been delivered, the carrier may retain the balance until his entire freight has been paid.

The act of December 14, 1863, gives carriers the right to sell goods in satisfaction of their liens for charges upon the goods, where the person liable to pay the charges fails or refuses to pay within sixty days after demand made. The

costs of sale, together with the cost of advertising notice of the sale, as required by the act, are taken out of the proceeds in addition to the amount of the carrier's charges. This act is set forth in Chapter XXXVII, subdivision (A).

(G) Termination of liability; delivery by carrier.

In order to terminate his liability, the carrier is bound to make proper delivery of the goods at their destination. In some cases, the carrier ceases to be liable as insurer where the goods have arrived at their destination and it is necessary for the carrier to store them in a warehouse. Where the goods are so stored to await the consignee's convenience, the carrier's liability is that of a warehouseman, who is bound only to ordinary care. Note what is said under subdivision (C) about delivery to connecting carriers.

The carrier must make delivery to the proper person; that is to say, to the consignee. Delivery must be made, not only to the proper person, but also at a reasonable time, at a proper place, and in a proper manner. If he does not deliver to the right person, he is liable to such person, even though he has made an honest mistake. This duty gives the carrier the right to require very clear proofs of identity of the consignee; and if he has a reasonable doubt as to whether the person claiming the goods is entitled to them, he is justified in refusing to deliver to him until the claimant's right is established. In making such refusal, the carrier must have a reasonable excuse, and must act in good faith solely with a view to the proper delivery of the goods. Where the carrier holds the goods at the point of their destination, and becomes a mere warehouseman for the convenience of the consignee, he is not held to such strict liability in regard to their delivery. He must use all reasonable care, however, even where he is only a warehouseman. The old rule was that all carriers must make personal delivery to the consignee. The modern rule is that a railroad company can only be required to deposit the goods in safety at the end of the journey to await delivery to the consignee. The arrivals of goods by railroad are so numerous and frequent that it would be practically impossible

for the carrier to send a special notice to each consignee, of each shipment of goods as it arrives. Such notices are not required of a railroad company. Anyhow, the consignee is likely to know when the goods will arrive, for usually he gets word from the consignor, or in some other manner. The courts take the view that when the goods have been deposited by a railroad company in a place of safety, to await delivery to the consignee when he calls for them, the contract as common carrier is at an end. Until the consignee calls for the goods, the railroad company is merely a warehouseman, and is liable only to use ordinary care in looking after the goods.

Express companies do a different business from railroad companies, and carry small and valuable parcels; hence, they are not entitled to require the consignee to call for the goods. Express companies undertake to carry a class of goods not suitable for freight, and their undertaking is to make a personal delivery of the goods to the consignee. The law holds them to this undertaking very strictly. However, at unimportant way stations they need only notify the consignee, and give him a reasonable time to call for the goods.

(H) Baggage.

The act of April 11, 1867, provides that "each passenger upon a railroad shall have the right to have carried in a car or place provided for that purpose in the train in which he or she may be a passenger, his or her personal clothing not exceeding, inclusive of the trunk or box in which it may be contained, 100 pounds in weight and \$300 in value. No railroad company shall under any circumstances be liable for loss or damage to any baggage or property belonging to any such passenger over the sum of said \$300, unless it shall be proved that the excess in value thereof over that sum was truly declared to the agents of the company at the time of its delivery for transportation, and the sum charged by the railroad company for transportation, over and above passage fare, was paid: Provided, however, that said declaration shall not relieve the claimant from proving the actual value of the article alleged

to have been lost or damaged; but in no event shall there be any recovery beyond the value thus declared. No railroad company providing a car or other place for the deposit of passengers' baggage shall under any circumstance be liable for loss or damage to any articles or property whatsoever not there deposited by the passenger, or which are placed by him or her in the car in which he or she is to be transported."

In *Brown v. C. & A. Railroad Co.* (1877), 83 Pa. 316, it is held that the act of 1867 does not apply where baggage is carried by a foreign corporation in another state. The plaintiff purchased from the defendant company, at its Philadelphia office, a ticket to Atlantic City, and the company received his trunk and checked it to the same destination. The trunk was lost while in the possession of the company, and the Supreme Court upheld a judgment for the plaintiff for \$1,300. The act of 1867 was not applicable to the case, for the law of New Jersey, *the place where the contract was to be performed*, governed the parties.

The carrier ordinarily is liable to use the same degree of care respecting the passenger's baggage as he is respecting goods sent by freight. There is no hard and fast rule as to what may be considered "baggage." What may be "baggage" for one person may not be for another. To some extent the question is similar to that of "necessaries," which we considered when treating the subject of contracts that can be enforced against a minor. By baggage is meant, such articles of personal convenience as are usually carried by passengers for their personal use, as distinguished from merchandise, which does not come under the head of baggage. In one case it was said that baggage is not limited to what every man deems essential to his comfort, but it includes what is usually carried as baggage. In an English case the court said that "whatever a passenger takes with him for his personal use or convenience, according to the habits or wants of the particular class to which he belongs, either with reference to the immediate necessities or to the ultimate purpose of the journey, must be considered as personal luggage. This would include not only all articles of apparel, whether for use or ornament,

but also the guncase or the fishing apparatus of the sportsman, the easel of the artist on a sketching tour, or the books of the student, and other articles of an analogous character, the use of which is personal to the traveler, and the taking of which has arisen from the fact of his journeying. * * * What is carried for the purposes of business, such as merchandise or the like, or for larger or ulterior purposes, such as articles of furniture or household goods, would not come within the description of ordinary luggage, unless accepted as such by the carrier."

In a Pennsylvania case it was held that a carpenter's tools were a reasonable part of his baggage. In another case, recovery was allowed for the value of a wife's jewelry. An amount of money which a passenger carries in his trunk for traveling expenses, and for his personal use, is considered as baggage, if the money is not in excess of what a prudent person would carry for such purposes. Wearing apparel carried for future use is treated as baggage, even though it is intended for other members of the passenger's family. The passenger is often allowed to retain partial control over his baggage and to use it for the purposes of the journey, but, notwithstanding such control of a passenger, the carrier is liable as the insurer of the baggage, in the absence of a statute or an agreement restricting his liability.

The carrier is not bound to act as a nurse or guardian for a passenger, and if a passenger carries his overcoat on his arm when he enters a coach, and leaves it behind him in the seat when he comes out, the carrier is not liable. In such a case the overcoat is not treated as baggage, but as part of the passenger's wearing apparel. In a case where the facts appeared as above mentioned the court said, "the passenger must at least assume responsibility of taking ordinary care of himself, including the wearing apparel about his person."

A passenger on a steamship may usually take his baggage into his stateroom, and, if it is there lost through no negligence of his, the carrier is liable as an insurer. Generally the passenger's baggage is taken into his stateroom at his own risk, because the steamship company makes a stipulation to that

effect. Such a stipulation seems to be reasonable, and the company is then liable only for its negligence.

The carrier has a lien upon the passenger's baggage for payment of the price of carriage, but he has no lien upon the wearing apparel that the passenger is wearing, or anything which the passenger keeps in his possession for his own personal use.

PART II

SALES OF PERSONAL PROPERTY

CHAPTER XL.

THE DEFINITION OF A SALE, AND DISTINCTIONS BETWEEN SALES AND BAILMENTS.

Throughout the following chapters a great deal will be said about the title to property. When a sale actually takes place the title is transferred from the seller to the buyer. The buyer becomes the owner of the property sold. Many important legal questions hinge upon the ownership of property at a given time. We must, therefore, understand exactly when the transfer takes place. Most of the cases to be cited relate to sales of tangible articles of personal property, such as horses or machinery. The principles stated, however, usually apply also to the sales of intangible personal property. For instance, if B owes you money, you may sell your claim against him to C. What you sell is a right of action, but it is your property, and may be transferred to C. Likewise, an inventor who receives a patent may sell it to a third party. His patent is an intangible property right secured to him by the United States patent laws. Again, an author, who has obtained a copyright under the national copyright law, has a species of intangible property which he may sell to another. These rights may not only be sold, but they may be transferred by other kinds of contracts. For instance, the holder of a patent may grant a license to another for the use of the patent during a limited time and within a limited territory. Labels, trade-marks, trade names, stamps, designs, devices, shop-marks and forms of advertisement may become the property of particular individuals, and the owners of them are protected, under cer-

tain conditions, by the Pennsylvania statute of June 20, 1901. See the case of *Brewing Co. v. Koenig* (1906), 30 Super. 618.

A sale is defined as a contract to pass rights of property for money which the buyer pays or promises to pay to the seller for the thing bought. The word "vending" is sometimes used instead of the word "selling," and the seller is called the "vendor," while the buyer is called the "vendee." As a sale is the transfer of the property in a thing for a money consideration, the subject of sales covers sales of real estate and sales of personal property. A sale, being a contract, is subject to the rules of contract law. Where the agreement of sale provides that the property in the thing sold is to be thereby transferred from the seller to the buyer, the title passes at once, and the sale is called an *executed* contract of sale. Where the agreement provides that the property in the thing shall be transferred from the seller to the buyer at a future time or on the performance of a condition, it is called an *executory* contract of sale. The parties to the contract are the seller and the buyer. In determining whether there is a valid contract of sale, one must look first to see whether the five elements necessary to every contract are present, and then one must inquire if the following three requisites are present in the agreement: first, a thing, the subject of the agreement, which is owned in most cases by the seller; second, an agreement by the parties that the property in the thing is transferred or is to be transferred from the seller to the buyer; third, payment, or an agreement for payment, of a price in money by the buyer to the seller. No writing is necessary to make a contract for the sale of personal property legally valid. It may be made in writing, or verbally, or it may be implied from the conduct of the parties.

A bailment of property should be distinguished from a sale, for while the bailment gives the bailee possession of the property, the title to it does not pass to the bailee by the contract, but remains in the bailor. The bailee gets possession of the property, but no ownership of it. For instance, when property is pledged for a loan the ownership remains in the pledgor, the person who pawns it, and possession only is trans-

ferred to the pledgee, who loans the money on the security of the thing pledged. The pledgee has a right to hold the property to secure his loan, but the contract of pledge does not make him owner of it.

The question whether a given transaction is a sale or a bailment of a certain article is not always easy to answer. Everybody knows the distinction between a sale, involving an outright transfer of ownership in an article, on the one hand, and the hiring or pledging or other bailment of the same article, on the other hand. These different transactions are usually quite simple, but sometimes they are confused with one another. Suppose a pledge agreement provides that under certain circumstances the person who advances the money, called the pledgee, shall become the owner of the property. It may be difficult to determine in a court of law at just what time the pledge turns into a sale. Take another case. Frequently, in order to protect the seller of property, the contract is so drawn up that title is not to pass until the last instalment of the purchase price is paid to the seller. These contracts usually provide that title shall be retained in the seller, and, on payment of the purchase money in full, it shall thereupon pass to the purchaser. This particular kind of agreement has caused endless trouble in the courts of Pennsylvania and elsewhere. If the purchaser is treated in the contract as the real owner of the property, and after getting possession of the goods, sells them to an innocent third party, it seems wrong to allow the original owner of the goods to claim them from the third party. His arrangement with the first person appears to be an out and out sale, coupled with a device to give him a lien on the property for unpaid purchase money. In such cases the court will uphold the third party as against the former owner of the goods, who claims that the transaction is not a conditional sale, but merely a bailment.

This does not mean that two parties may not validly agree that the owner of goods shall transfer possession of them on a certain rental to the other party, and that the other party shall have the option of buying the goods and thus getting ownership as well as possession at some time in the future. Suppose

that a man who owns a horse hires it to a friend for two months, and gives his friend the option of buying the horse at the end of that term, and letting the two months' hire of the horse go towards the purchase price if the friend determines to buy. This is a valid bailment with an agreement for a possible sale at the end of two months. If the bailee fraudulently sells the horse before the two months are up to a third party, the latter gets no title.

There are, therefore, two classes of cases to be distinguished. First, cases where there is a bailment contract between the parties, to be followed later by a sale, in accordance with the conditions agreed upon by them. This is usually valid. Second, cases where an immediate sale is really intended and agreed upon by the parties, and the purchaser gets possession and gets the right to exercise full ownership over the property, but the seller's attorney tries, by some transparent legal device, to enable the seller in case of future trouble to seize the property and save himself from loss. This the law does not encourage. The owner of property who sells it to another, and delivers possession of it, must take the risk of the other person's failing to pay him. It is unfair for him to try afterwards to defeat the rights of the purchaser's creditors or other innocent third parties by saying that the purchaser has no title. In cases like *Coble v. Nonemaker* (1875), 78 Pa. 501, chattel mortgages have been sustained as against parties who were aware of their existence, but their utility is virtually confined to the cases mentioned in Chapter XXXVIII. See *Fry v. Miller* (1863), 45 Pa. 441. If a man has the title to a certain article of personal property, and has that article also in his possession, he cannot hold the title and the possession, and at the same time give another a valid mortgage or lien on the article, except in the cases where chattel mortgages are valid. He cannot, under such circumstances, give a lien even to the person who has sold the article to him on credit, as security for the payment of the purchase money. Suppose you own a horse, and agree to sell it for \$200 C. O. D. and later the purchaser says, "I have not the money ready, as I agreed, but deliver the horse, and your \$200 shall be a lien

against it." If you deliver the horse, and the purchaser sells it to an innocent third party, your claim against it is gone. Likewise, if the purchaser fails, and his assignee takes possession of the horse, you can neither claim the horse back nor secure a preference over other creditors for your bill of \$200 out of the proceeds of the sale of it.

An agreement by which the purchaser gets possession of goods, but the transfer of the title to him is dependent upon his paying for them, is called a conditional sale. This agreement to retain title in the conditional seller is binding between the parties, but not always as against third persons. The courts hold that a conditional purchaser may, before payment of the purchase money, transfer a good title to one who buys the goods from him, if the latter does not know about the rights of the conditional seller. *Forrest v. Nelson* (1885), 108 Pa. 481. A distinction should be noted between the position of one who buys at private sale from the conditional purchaser, and the position of one who buys at a sheriff's sale under legal proceedings against the conditional purchaser. In the first case, the one buying at private sale cannot hold the property as against the conditional seller, if he knew about the agreement reserving title in the latter. In the second case, the one buying at sheriff's sale can hold the property, although he knew of the prior transaction. *Seeley v. Garey* (1885), 109 Pa. 301. See also *Krause v. Commonwealth* (1880), 93 Pa. 418.

This rule has inconvenienced instalment houses and other business concerns which want to keep a legal hold on goods delivered to customers until the customers shall have fully paid for them. To overcome the effect of the rule, merchants have resorted to various legal devices, as by giving the transaction the appearance of a lease or consignment, or by making the customer a trustee for the merchant, who thus keeps a string tied to his goods. The courts will unmask these transactions if the contract of lease (or other contract which is substituted for a conditional sale contract) is not carefully drawn. Judges recognize, however, the commercial demand for contracts which will protect an instalment house or other concern dealing with people whose credit is bad, and will uphold such contracts when they are properly prepared. Most instalment

contracts as well as others of a similar nature are got up to appear quite like a lease. Many of them contain a provision that, at the end of the term of the lease, if the lessee has fully paid all of the so-called rental, he shall for the further sum of one cent become the owner of the property.

Let us contrast a case where the contract was awkwardly drawn, and hence failed to protect the creditor, with several cases in which skilfully worded contracts have produced the desired results.

In the case of *Laundry Machinery Co. v. Fromuth* (1900), 15 Super. 339, it appeared that the Henrici Laundry Machinery Company had delivered certain machinery to Bird & Wilson. The written contract between them provided that "this property is borrowed by us and is to belong to the Henrici Machinery Company until the price of its purchase is paid as per memorandum above, and then becomes the property of the borrower and is lent until default is made in either payment, to be held by the borrower and no other, and upon the condition that the borrower is to return it to Henrici Laundry Machinery Company upon such default. Notes and drafts, if given, are not considered as payment until they are paid, and all payments are to be forfeited by non-payment of the balance at the time stated in this agreement." The machinery while in the possession of Bird & Wilson was levied on in a suit brought by August Fromuth against them. The Henrici Company claimed the machinery, but it was proved that the goods were charged against Bird & Wilson on their books as if sold. Some of the machinery had been so charged before being delivered to Bird & Wilson and before the signing of the contract.

The court held that title had passed to Bird & Wilson. The contract was a thinly veiled attempt to preserve a lien on goods. The attempt to make the relation between the parties that of bailor and bailee, until the purchase price should be paid, failed, because the ordinary features of a bailment contract were not present. No time was fixed for the duration of the bailment. Nothing was to be paid for the use of the machinery while the bailment relation should continue, that is,

while the machinery should continue to be merely "borrowed." No control over the property was reserved by the machinery company. A bailment agreement in this kind of transaction should provide a certain sum of money to be paid by the bailee, and should give the bailor the right to seize his property again upon the bailee's default in this respect. The money payable from time to time should be called "rental" or some other word applicable to a bailment. The contract in question referred to the "price of its purchase," which is a term indicating a sale, rather than a bailment. Furthermore, the books of account should carry out the same idea, and the bailee should be charged as such. Payments by him should be credited as payments of "rental," and not as payments on account of a purchase.

An instalment contract which was successfully disguised as a bailment figured in the case of *Lippincott & Co. v. Scott* (1901), 198 Pa. 283. Lippincott & Co. delivered a soda water fountain to Kuhn under a contract which stated that Kuhn was not the owner of the fountain, title being retained in Lippincott & Co. Instalment notes were given for certain fixed sums to be paid every month, and it was agreed that the fountain should be leased for thirty-seven months, and not removed from Kuhn's place of business. In default of any monthly payment it was to be redelivered to Lippincott & Co. Lippincott & Co. agreed that if Kuhn desired to purchase the fountain at the expiration of the thirty-seven months they would make and deliver to him "a bill of sale therefor upon payment of such sum as will, with previous payments of hire, amount to \$4,000." Scott claimed the fountain under a sheriff's sale of Kuhn's property. Lippincott & Co. resisted this claim on the ground that Kuhn had not become the owner of the fountain when the sheriff's sale was made. The court upheld Lippincott & Co., and decided that until Kuhn should pay the entire sum of \$4,000, the contract operated to retain the ownership in Lippincott & Co.

In the case of *Potter v. Stetson* (1899), 11 Super. 627, the following excellent form of agreement was decided to create a bailment, and not an immediate sale. This contract was prepared for the benefit of N. Stetson & Co., piano manu-

facturers. It enabled them to retain ownership of their pianos after delivering them to customers on the instalment plan:

“N. Stetson & Co. Lease No. 79.

“Notice.—No salesman, dealer or agent is permitted to make any verbal contract or promise that will in any way conflict with or qualify the terms, or written or printed conditions of this lease, or to give, or promise to give, any article, accommodation or service, not specified in this lease, and N. Stetson & Co. will not be responsible for any agreements or promises of any nature in connection with this transaction, that are not fully written on the face of this lease.

“This agreement, made this 27th day of January, A. D. 1894, between N. Stetson & Co., a corporation under the laws of the State of New Jersey, party of the first part, and John E. Potter, of 6509 Ellwood avenue, Philadelphia, party of the second part,

“Witnesseth, That the said party of the first part hath, and by these presents doth, let unto the party of the second part a Steinway & Sons’ upright No. 78,072, for the term of sixteen months and days from date, at the rental of \$700, \$200 to be paid through advertisements, \$30.00 upon the first day of February next, and \$30.00 on the first day of each month thereafter during the term, in advance.

“The party of the second part agrees that said instrument shall be placed in premises situate 6509 Ellwood avenue, and not to be removed therefrom without the written consent of the party of the first part, except in case of removal necessitated by danger from fire; and at the expiration or sooner determination of this lease to deliver up the said instrument to the said party of the first part, in good order, reasonable wear and tear excepted.

“The party of the second part agrees to cause the said instrument to be insured against loss by fire in a responsible insurance company, for the benefit of the party of the first part, during the said term.

“If the party of the second part promptly and fully performs all of the covenants on his part to be kept under this agreement, and desires to purchase the instrument, the party

of the first part agrees, upon the payment to them of the sum of 1-100 dollars [one cent] within thirty days after the expiration of the term, to deliver to the party of the second part a bill of sale of said instrument.

"If default is made by the party of the second part in keeping any of the covenants herein on his part to be performed, then the said bailment shall forthwith cease and determine, and it shall be lawful for the party of the first part to enter upon the premises where the instrument is kept and repossess themselves of same as though it had never been rented. And at their option it shall be lawful for them to file this lease or copy of the same in any court, together with an affidavit as to default, and to enter in such court such amicable action as may in their judgment be best adapted for the recovery of said instrument, without security or bond, and any attorney is hereby authorized to sign said amicable action for the party of the second part, and also to appear and confess judgment against said party in said action; and the clerk of said court is hereby requested by the party of the second part to enter said action and confession of judgment and issue such writs as are necessary to enable the party of the first part to obtain the said instrument by process of law, the said party of the second part hereby releasing and waiving to the officers of the law and all parties concerned, all errors and all rights of appeal and stay of execution.

"If such default does occur, and the party of the first part do not forthwith exercise their rights as above, such extension or indulgence shall not be considered in fact or in law as a waiver of any of such rights.

"This agreement is to be binding upon the heirs, executors, administrators, successors and assigns of all the parties hereto.

"Witness our hands and seals the day and year aforesaid:

"N. STETSON & Co. (L. S.)

"(per) A. VON BERMUTH.

"JOHN E. POTTER. (L. S.)

"Witness:

"CLARENCE SHANK."

Another method of protecting a capitalist is seen in the case of *Brown Bros. & Co. v. Billington* (1894), 163 Pa. 76. Sweeting, a bicycle dealer, obtained from Brown Bros. & Co. letters of credit, in order to buy bicycles abroad. The contract which Brown Bros. & Co. made with Sweeting provided that the bicycles should be shipped to them in the United States and as their property, bills of lading being made out in their name. Brown Bros. & Co. paid the drafts drawn on them by the sellers of the bicycles. Sweeting later received the bills of lading, signing a trust receipt, drawn up about as follows: "Received from Brown Bros. & Co. the following goods and merchandise, their property, specified in [details omitted] bill of lading, and in consideration thereof, I hereby agree to hold said goods in trust for them, and as their property, with liberty to sell the same for their account, and further agree, in case of sale, to hand the proceeds to them to apply against the acceptances of Brown, Shipley & Co. or Brown Bros. & Co. Brown Bros. & Co. may at any time cancel this trust and take possession of said goods, or of the proceeds of such of the same as may then have been sold, wherever the said goods or proceeds may then be found; and in the event of any suspension or failure or of the non-fulfilment of any obligation made under any credit issued by Brown Bros. & Co. or Brown, Shipley & Co. on my account, or of any indebtedness on my part to either of them, all obligations, acceptances, indebtedness and liabilities whatsoever shall thereupon, with or without notice, mature and become due and payable. The said goods while in my hands shall be fully insured against loss by fire." Billington, another creditor of Sweeting, issued execution against the bicycles as Sweeting's property, and Brown Bros. & Co. claimed the bicycles as their own. The court held that Sweeting was not the owner of the bicycles. He had possession of them merely as bailee or trustee for Brown Bros. & Co. See also the following cases: *Keystone Watch Case Co. v. Fourth St. Bank* (1900), 194 Pa. 535; *Stiles v. Seaton* (1901), 200 Pa. 114; *Electric Co. v. Brown* (1899), 193 Pa. 351.

CHAPTER XLI.

THE TRANSFER OF TITLE FROM SELLER TO PURCHASER.

In this chapter we shall consider, first, when the title passes by virtue of a contract of sale, and, second, what title is acquired by the purchaser. You cannot obtain a perfect legal title to real or personal property merely by getting some person to agree, verbally or in writing, to sell the property to you. Unless the seller has himself a good title, you do not usually obtain one through any contract of sale which he may make.

(A) When the title passes to the buyer.

When does the contract of sale pass rights of property from seller to buyer? The answer to this question usually determines who shall bear the loss in case the goods are destroyed by fire or other cause, for such risks usually follow the ownership of the goods. The contract of sale depends on the intention of the parties, and if they express their intention as to when title shall pass, that intention usually governs. In the absence of a direct expression as to when title shall pass, the courts adopt the most reasonable interpretation of what the parties probably had in mind under the particular circumstances of each case. Where the seller delivers the goods to the buyer personally the point of time when title passes to the buyer is generally fixed at the moment of delivery. Where the seller is to deliver the goods to a carrier for transportation to the buyer, the carrier is usually regarded as the buyer's agent, and hence title passes to the buyer when the seller delivers the goods to the carrier. Where the seller is bound to send the goods to the buyer, delivery to a common carrier is usually delivery to the buyer, and transfers the title. If, however, the seller undertakes to make the delivery himself at a distant place, thus assuming the risks of transportation, the carrier is his agent, and usually title does not pass until the delivery agreed upon is made. *Glass Co. v. Irwin & Co.* (1893), 153

Pa. 440. The letters *f. o. b.* have frequently guided the courts to the conclusion that the intention was to make delivery by the seller such a part of the seller's duties with respect to the goods as to postpone the passage of title until the time when the seller completes what he is to do with the goods, and finally delivers them *f. o. b.* at the place mentioned. The letters *f. o. b.*, nevertheless, may mean merely that the seller is to be charged with the cost of transportation to the place designated, and if this clearly appears, the general rule that delivery to the carrier passes title to the purchaser may apply. The letters *c. o. d.* are not decisive of the question when title passes. They indicate that the seller will insist on his lien for the purchase money. The delivery of a bill of lading or warehouse receipt is viewed as a symbolical delivery of the goods themselves, and usually passes the title to the purchaser.

Where there is merely a contract to purchase at a future time, no title passes when the contract is made. Where the seller is to manufacture the goods, or do some work on them, the title usually does not pass until the seller has completed what he is to do. While the time when title passes depends on the intention of the parties, and the title may pass to the purchaser before the goods are delivered to him, yet if the goods bought are part of a large quantity of similar property, there must be some specification as to which particular goods shall be set apart to fill the order, before any title can pass to the purchaser. The reason of this is that title refers to specific property, and until some particular goods are appropriated to the buyer's order he cannot be considered to have become the owner of any part of the goods. An exception to this rule exists in the case of such uniform articles as oil and wheat, for a man may become the owner of, say, 1,000 gallons of oil in a tank which contains 8,000 gallons without specification as to which gallons are sold to him. Where the goods are to be measured or inspected, and the final calculation of the price depends on the measurement or inspection, the title may pass before the measurement or inspection, if the parties clearly intend this. Unless otherwise agreed, the passage of title does not necessarily depend on the buyer's payment of the purchase

money: indeed, many buyers of goods fail to pay for them at all, but this failure standing by itself seldom gives a seller the right to reclaim possession if he has already delivered it to the buyer. The time of the specification and setting apart of the goods for the buyer is frequently the time when title passes to him.

(B) *What title passes to the buyer.*

What rights of property pass from seller to buyer? The general rule is that the seller cannot pass a better title than he has himself. This means that ordinarily only the owner of property can sell the right to that property. It means also that the measure of the seller's rights is the measure of what the buyer acquires. If the seller has pawned the article sold, the buyer purchases subject to the pawnbroker's right to hold the article as security for the loan to the seller, with interest and storage charges. It was shown, however, in the preceding chapter that a conditional purchaser may transfer a good title to an innocent third party, though as between the first seller and the conditional purchaser title has not passed to the latter. We shall see also that if the purchaser of goods permits them to remain in the seller's possession, a second innocent purchaser from the seller may be entitled to treat the seller as the real owner, although as between the seller and the first purchaser title has passed to the latter. The general rule, however, is that the buyer acquires only the seller's title.

In the case of *Hosack v. Weaver* (1795), 1 Yeates 478, William Hosack sued Henry Weaver for a gray stallion, which had been either lost or stolen out of his wagon in his yard at Winchester, Maryland. The plaintiff discovered the horse in the defendant's possession in Philadelphia, but the defendant founded his claim on a purchase from a man in the horse market in Philadelphia, *bona fide* and for a full consideration, and proved that the horse had been shown publicly there on two or three market days before the sale. Hosack won, for the court held that the owner of goods which have been lost or stolen may claim them even in the hands of an innocent purchaser for value. In the case of *Bradlee & Co. v. Whitney*

& *Kemmerer* (1885), 108 Pa. 362, Bradlee & Co. were compelled to pay a second time for coal which they had bought under the following circumstances: A. J. Cohen, a coal broker, obtained an order for coal from Bradlee & Co. He took it to Whitney & Kemmerer, who agreed to fill it, and to pay Cohen his commission when Bradlee & Co. should pay them. When the coal was delivered to Bradlee & Co., the bill of lading plainly showed that Whitney & Kemmerer were selling the coal, but Bradlee & Co. paid Cohen for it. Cohen absconded, and Whitney & Kemmerer sued for the purchase money. The court held that the purchasers should have seen who the owners were from the bill of lading. They knew that Cohen was without means, and Whitney & Kemmerer had not entrusted him with the possession of the coal. They consigned it in their own name, and although Cohen was their agent in a certain sense, they had not clothed him with the appearances of ownership. From this case it will be seen that the broker or other agent who negotiates the sale is not usually a party to the contract. The owner of the property for whom the agent acts is usually the seller.

An exception to the rule that the buyer acquires no clearer title than the seller had sometimes arises through the doctrine of estoppel, as appears in *O'Connor v. Clark* (1895), 170 Pa. 318. John O'Connor, who kept wagons for hire, engaged George Tracy as an employee. Tracy had been in the same business. O'Connor was having a wagon built, and ordered the builder to print on the wagon the words "George Tracy, Piano Mover," for O'Connor wanted to retain the business which Tracy had built up for himself. Tracy offered the wagon, together with the horse which pulled it, to John Clark for \$125. Clark, before paying the money, went with Tracy to a police station and a saloon, where Tracy was identified as the George Tracy whose name was on the wagon. The horse and wagon were delivered to Clark, and O'Connor sued Clark to recover them.

The court held that where one of two innocent persons must suffer loss by reason of a third person's fraud, the loss should fall on him by whose act or omission the wrongdoer

has been enabled to commit the fraud. The owner of wagons should be particularly careful in this respect, for they are so easily moved about that the temptation to dispose of them fraudulently is stronger than in the case of many other kinds of property.

Another application of the doctrine of estoppel sometimes occurs when the purchaser of goods permits them to remain in the seller's possession. In the preceding chapter we saw about conditional sales. The condition that title shall not pass to the purchaser until he pays the seller for the goods delivered, is not legally valid as against innocent third parties dealing with the purchaser. Now reverse the situation, and imagine the following state of facts: Suppose a man has a cow on his farm, which he sells to another farmer, but the cow is allowed to remain in the seller's barn, although the purchaser has paid for it. Suppose that the seller who retains possession of the cow is dishonest, and sells it over again to still another farmer, who pays for it, and leads the cow off. Both purchasers have acted in good faith, and a lawsuit is started to determine which of them is to get the cow. The first purchaser asserts that title passed to him, and that the original owner of the cow had nothing to sell. The second purchaser objects that it was unfair to him that the cow should have been allowed to remain with the original owner, for nobody under these circumstances would suppose that he had sold it. As between these two parties, the second purchaser would be preferred, for the rule is that the first purchaser should obtain possession of the cow, and if he leaves it with the seller, he does so at his own risk. Leaving goods with the seller is likely to mislead subsequent purchasers into believing the seller's statement that he still owns them. This rule is for the protection of third parties dealing with the seller, while the similar rule as to conditional sales is for the protection of third parties dealing with the purchaser. *Kendig v. Binkley* (1899), 10 Super. 463.

A distinction should be noted between the position of a subsequent purchaser at private sale, and the position of a purchaser at a sheriff's sale under legal proceedings against

the seller, whom the first purchaser has allowed to retain possession of the goods. In the first case, the subsequent purchaser cannot hold the property as against the first purchaser, if he knew of the prior sale. In the second case, the purchaser at sheriff's sale can hold the property, although he knew of the prior sale, if the sheriff's sale is under legal proceedings upon a debt contracted *before* the transaction with the first purchaser, who let the seller retain possession. That transaction is presumed to be fraudulent as against existing creditors of the seller. Suppose, however, that the sheriff's sale is under legal proceedings upon a debt contracted *after* the transaction with the first purchaser, and that the purchaser at the sheriff's sale knows about the prior transaction. In that case, he can hold the property as against the first purchaser only by actually proving that the latter permitted the seller to retain possession with a definite intention of defeating the rights of subsequent creditors. *Ditman v. Raule* (1889), 124 Pa. 225. See also *Stephens v. Gifford* (1890), 137 Pa. 219, and *White v. Gunn* (1903), 205 Pa. 229.

Taking up the rule which protects an innocent second purchaser where the first purchaser has allowed the seller to remain in possession of the goods, we may refer to the objection that title has been passed to the first purchaser. How, therefore, can a seller pass the right of property to the second purchaser? The answer is that the first purchaser got title as between himself and the seller, but he has acted imprudently in allowing the seller to retain possession of the goods, so that he will not be allowed to assert his title as against a subsequent purchaser. The rule just mentioned is usually applied where the seller has possession at the time of the sale, and retains it after the sale. If he has surrendered possession to the first purchaser before the second purchaser comes along, the mere fact that the goods remained for a while in the seller's hands after the first sale does not give the second purchaser a right to obtain the goods from the first purchaser. The first purchaser secured possession before his delay in doing so helped to mislead the second purchaser. Suppose the property is left in the seller's hands by the first purchaser, and

then it is sold to the second purchaser, who also leaves it in the seller's hands. Later the seller delivers it to the first purchaser. In that case the second purchaser would have no right to the property, for he is not more vigilant than the first purchaser. Where the same thing is sold to two different purchasers, and the second purchaser is without notice of the first sale, he who first gets possession of the property will be protected by the courts. In this case both parties are equally careless, and the one who gets possession first is in the stronger position. Suppose, to take a new case, the first purchaser takes possession of the goods, knowing the rule which we have been studying, and fearing that the seller will sell to another. As soon as he gets possession he returns the goods to the seller, considering that he has complied with the rule as to getting possession, and the seller having been restored to the possession of the goods, turns around and sells them to an innocent second purchaser. In that case there has been merely a formal delivery. The purchaser has complied with what he imagines to be the letter of the law. This mere technical compliance is not enough, for it does not answer the real purpose of the rule, and the seller is just as much enabled to mislead a subsequent purchaser. The subsequent purchaser who obtains possession of the goods is, therefore, entitled to hold them as against the first purchaser.

Needless to say, the law does not empower everybody who has the mere possession of goods to pass the title to them so as to defeat the rights of property of the real owner. If you own a bicycle and lend it to a friend, and the friend sells it to an innocent third party, you can get your bicycle back if you can find it. The mere possession of the bicycle by your friend is not enough to clothe him with a right to pass the title to it. If that were the case, it would be imprudent for the owner of any property to let it go out of his hands for a moment. We have seen, however, that a purchaser who has just bought property may lose his right to it as against a subsequent purchaser, if he lets it stay in the seller's hands. The reason of this rule is that third persons may be easily deceived by the seller who has formerly had not only possession but also ownership.

We have seen that if the purchaser gets possession, and immediately delivers it back to the seller, the mere formal transfer of possession will not defeat the rule, and a subsequent purchaser who obtains possession of the goods from the seller in good faith can hold the goods as against the first purchaser. Suppose now that the goods have remained for some little time in the first purchaser's hands, and then he delivers them back to the seller. The transfer of possession was more than a mere ruse to evade the rule for the protection of a subsequent purchaser. When the seller finally gets the goods back, either to store them for the first purchaser, or to manufacture them into some finished product, or as security for a loan, suppose he turns around and sells the goods to a second purchaser. In that case the rule does not apply, for the possession has not remained uninterruptedly in the seller. It has been transferred to the first purchaser, who has afterwards transferred it back to the seller on a contract of bailment. The second purchaser gets no title from the seller, for the transaction is the same as if the first purchaser had stored the goods with an entirely new party, and the new party had dishonestly undertaken to sell them as his own property.

If the first purchaser is in possession of the goods at the time of sale, as where a bailee exercises an option to buy, no question of delivery of possession is likely to arise in favor of a second purchaser, for the first purchaser has possession already. A difficult question faces us where the property at the time of sale is in possession of neither seller nor purchaser. In such case the first purchaser will be all right if he gets the warehouse receipt or bill of lading, and even a bill of sale is usually sufficient to protect the first purchaser against the consequences of a subsequent sale by the original seller to an innocent second purchaser. A purchaser of goods which are in the hands of a third party may find it advantageous to give prompt notice of the purchase to the third party.

Several other cases may be mentioned where the party who makes sale of goods confers upon the purchaser a better title than he had himself. If judgment is recovered against the owner of property, real or personal, and the sheriff

sells this property to satisfy the judgment, the same title that the owner has usually passes to a purchaser at the sheriff's sale. The sheriff, who makes the sale, and who signs a deed for any real estate sold by him, has no title himself. It may be said, however, that he is an agent designated by law to act on behalf of the owner, even against the owner's wishes. Purchasers at sheriffs' sales should bear in mind that they usually acquire no better title than was possessed by the person against whom the legal proceedings are being taken. For instance, if judgment is recovered by A against B, and the sheriff seizes the goods of X, and sells them in the belief that they are B's, he cannot usually transfer a good title to the purchaser. If X has notice of the sale, he should take prompt measures to assert his rights, and prevent innocent third persons from being deceived. He should, if possible, have it announced before his property is put up that it does not belong to B, and that a mistake has been made. See also the act of April 26, 1887, providing for the sale, without the owner's knowledge, of certain animals which have strayed away.

We shall see in the next chapter that a purchaser who obtains goods by fraud has usually only a voidable title. If he sells them to an innocent third person, the latter usually acquires an entirely valid title. This makes another exception to the rule that the purchaser gets no better title than the seller had himself. Still another exception exists when negotiable instruments are sold. One of the essential features of such instruments, as explained in the tenth chapter, is that an innocent holder for value in due course of business is not subject to most defenses which would have been good as against the payee or other previous holders.

CHAPTER XLII.

THE RIGHTS OF THE SELLER OF PERSONAL PROPERTY.

The seller's rights depend largely upon the terms of the agreement which he has made with the buyer. We need not repeat here what has been covered in the first book, which deals with contracts in general. The present chapter, therefore, will be devoted to considering certain phases of contract law which particularly concern the sale of personal property. Many mistakenly believe that if they sell goods on credit, they have a right to take them back if the purchaser fails to pay. The principles of contract law show us, however, that where a seller has delivered goods, and given the purchaser, say, thirty days within which to pay him, his only right under the contract is to try to force the purchaser to pay. The courts will not set the contract aside, and enable him to recover his goods, unless it was specially agreed that this might be done if the purchaser should fail to pay. Nevertheless, where the purchaser has obtained credit by false representations, the contract is tainted with fraud, and may be set aside on that ground. The seller's rights to be treated in this chapter are three in number. First, his right to set aside the contract if the buyer has committed fraud. Second, his right to refuse delivery until the purchase money is paid. This is called the seller's lien for the purchase money. It is frequently waived by the seller, and many contracts of sale specifically provide that the buyer shall get the goods on credit. Third, his right of stoppage in transit. We shall consider these in the order named.

(A) The seller's right to set the contract aside on the ground of fraud.

Let us imagine that the owner of goods is defrauded into agreeing to sell them by the purchaser's false representations. If the seller learns of the fraud before delivering posses-

sion of the goods, he may refuse to go ahead with the transaction. He has only himself to blame if he subsequently delivers them, and cannot afterwards rely upon the fraud to have the sale set aside and possession of the goods restored to him. Take the usual case, however, where the seller after he has delivered goods on credit learns that the buyer's statements as to his financial condition were fraudulent. What is the seller to do? The buyer has a voidable title. If the buyer has in the meantime sold the goods to an innocent third party, that innocent third party takes a good title, and the original seller cannot reclaim the goods from him. Imagine then that the goods are still in the buyer's hands. If the seller goes to the buyer, and the latter induces him to take a note for the money due, the seller, by accepting the note, waives his right to have the sale set aside on the ground of fraud. In the same way if the seller brings suit for the money due against the buyer, he thereby affirms the contract, and relies only on his usual right as seller to sue for the purchase money. The seller should disaffirm the sale, alleging that it was not a genuine contract, because it lacked reality of consent, the fourth element necessary to every contract. He should bring an action of replevin, and have the sheriff seize the goods, on the ground that he has the right to have the sale annulled, and the goods restored to him.

In order to defeat an alleged contract on the ground that there was no reality of consent, the misrepresentations must have been material. They must have been misrepresentations of some important fact. Moreover, they must have been relied upon by the seller, so that he can afterwards say with reasonable plausibility that if he had known the real facts, and not trusted to the purchaser's misrepresentations, he would never have sold the goods. In Pennsylvania *the mere fact that the purchaser is insolvent* at the time of the sale, and says nothing about it to the seller, is not sufficient to enable the latter to regain possession of the goods after he has delivered them to the purchaser. If the purchaser assures the seller that he is solvent, when he is really not so,

that is a misrepresentation of an existing fact, which is sufficient to enable the sale to be set aside. A mere statement of opinion or belief by the purchaser which proves incorrect, is insufficient to enable the seller to obtain his goods again. *The fact that the purchaser did not intend to pay for the goods when he bought them, is not, of itself, sufficient.* From all this you can see that the seller should learn whatever he can about the advisability of selling on credit before he lets the goods go out of his possession, for it is no easy matter to get them back afterwards, even where the rights of innocent third parties have not intervened.

There is one class of cases in which it is held that absolutely no title passes to the purchaser who has made fraudulent misrepresentations. This is where he falsely impersonates another. If the seller, believing him to be that other person, intends to sell to the party who is impersonated, the contract is void. There was no intention to transfer title to the impersonator who obtained the goods.

The act of March 28, 1905, was passed to prevent merchants from suddenly disposing of their goods in bulk, and refusing to pay their creditors. It directs that the sale of the whole or a large part of a stock of merchandise or fixtures, otherwise than in the ordinary course of trade shall be fraudulent and voidable as against the seller's creditors, unless the purchaser shall in good faith get a list of the creditors from the seller, and notify each of them five days before the conclusion of the sale. The act directs that proceedings must be brought against the purchaser within ninety days, in order to set such a sale aside on the ground that notice was not given to the creditors. The act further provides that if the seller wilfully gives a false list to the purchaser or induces the sale by refusing to answer the purchaser's inquiries, or by pretending ignorance of the matters called for by the purchaser's inquiries, the seller shall on conviction be sentenced to pay a fine not exceeding \$5,000, or to be imprisoned not exceeding six months, or both. This act is very important. Of course, it does not apply to sales by assignees for the benefit of creditors, or by receivers or trustees.

(B) The seller's lien for the purchase money.

Where nothing is said about the terms of sale, and there is no custom to the contrary, a sale of goods is supposed to be made for spot cash. On the other hand where the seller agrees to give the buyer, say, thirty or sixty days' credit, in the absence of express terms or a custom to the contrary, the seller is supposed to be willing to deliver the goods to the buyer and to trust for payment to the buyer's credit. Where there is no express or implied agreement to give credit, the buyer cannot demand the goods without having the money ready to pay for them. The idea that payment is to be contemporaneous with delivery enters into the contract, and the seller may hold the goods until paid for them. Even though title may have passed to the buyer, the seller has a lien on the goods to secure the payment of the purchase money, which gives him the right to keep them until he is paid in full, unless he has agreed to sell on credit. He is at perfect liberty to abandon this lien by delivering the goods, but his security is gone as soon as the buyer gets the goods to take them away.

If it is understood that the goods are to be sold *c. o. d.* and the buyer fraudulently violates the contract by getting possession of the goods from some clerk who does not know of the agreement, the seller may, if he acts promptly, repossess himself of the goods. The lien which he had on them to secure payment of the purchase money has not been waived by him. Suppose the title has passed to the buyer, but the seller is to hold the goods until the buyer needs them. If the sale is not on credit, this would be a typical case where the title passes, while the seller still keeps a lien on the goods, so that he need not surrender them until his bill is paid. Even if the seller charges the buyer for storing the goods, this does not defeat the seller's lien, unless it is understood between the parties that the buyer need not pay on delivery, but is to have credit. Suppose, however, that the buyer is given thirty days' credit. Suppose the title has passed to him, and the thirty days expire before the buyer has exercised his right to remove the goods. At the end of thirty days the period of

credit is up, and the lien of the seller revives, so that it is too late for the buyer afterwards to demand the goods, unless he has the cash to pay for them. Suppose, to take another case, the seller waives his lien as to a part of the goods by handing them over to the buyer without insisting on spot cash. This does not destroy his lien as to the goods which the seller retains, and he may hold this balance of the goods in his possession as security for the entire bill.

In studying the point as to the exact time when title is passed from the seller to the buyer, we noted the general rule that usually delivery by the seller to a transportation company, which is to carry the goods to the buyer, is considered delivery to the buyer, and title passes at that moment. Applying this in the present case, we deduce the rule that in general the seller's lien to secure payment of the purchase money is gone as soon as he delivers the goods to a railroad company or other common carrier, which is to take them to the buyer. Where, however, in exceptional cases, the agreement of sale is such as to reserve the title in the seller until the actual delivery of the goods at the buyer's place of business, the agreement prolongs the seller's lien upon the goods. In such cases the transportation company holds the goods as the seller's agent, and the seller has not legally parted with possession of them. He may recover the goods from the railroad company and hold them as security at any time before they are delivered to the buyer.

The lien which the seller claims in this way does not destroy the contract, for it is in pursuance of an express or implied term of the contract that the seller may keep the goods until he is paid, as security for the purchase money. This is called the seller's lien for the purchase money, and it exists in almost every case where there is no express or implied agreement that the goods shall be sold on credit.

(C) The seller's right of stoppage in transit.

We come now to consider another right which the seller of personalty enjoys, and which must not be confused with his right of lien to secure the payment of the purchase money.

This is the right of stoppage in transit. We have seen that where goods are delivered to a railroad company or other common carrier, the common carrier is usually considered to be the buyer's agent, and the seller's lien to secure his purchase money terminates as soon as he delivers the goods to the buyer's agent. Suppose that after he has delivered the goods to the railroad company he learns that the buyer has just failed. Would it not be a hardship to have those goods transported to the buyer's city, and put with the buyer's stock, since the seller would probably never be paid for them? The law under those circumstances gives the seller the right of stoppage in transit, even though title has passed to the buyer, and the goods have been delivered to the carrier as the buyer's agent. It exists only when the buyer has become insolvent. If the buyer has stopped paying his debts as they fall due, or if it appears in any way that he cannot meet his obligations, the seller may notify the carrier not to deliver the goods. The other right which we were considering before, namely, the seller's lien on the goods for the purchase money, exists irrespectively of the financial condition of the buyer.

The right of stoppage exists in favor of the seller of the goods during the entire period when the goods are being transported, but ends as soon as the transportation comes to an end, and the buyer or his agent receives them. If, however, the buyer has transferred the bill of lading to an innocent holder for value, the latter's rights are ordinarily superior to those of the seller. The mere fact that the goods are sold on credit, or that a note has been taken for the value of the goods by the seller, does not deprive the seller of this right of stoppage in transit. The right of stoppage in transit is to secure to the seller the payment for the particular goods which are being transported. He cannot exercise the right if he has been paid for those goods, merely because the purchaser may owe him money on other accounts. Even the seller's lien, which we considered before, enabling him to retain goods as security for his purchase money, where he has not delivered them at all, is given to him to enforce payment only for the particular goods in question. The goods cannot

be held for other accounts, but part of a single bill of goods may be held as security for payment of the entire bill, though some of the goods have already been delivered to the buyer.

CHAPTER XLIII.

THE RIGHTS OF THE PURCHASER OF PERSONAL PROPERTY.

We may consider the purchaser's rights under two heads, first, his right to make the seller deliver goods of a certain quality, and, second, his right to insist that a good title to the property purchased must be transferred to him. There are numerous other rights which a purchaser may obtain under a contract of sale, but they do not require special treatment here. For instance, we saw in the first book that in mercantile transactions a provision as to the time of performing a contract is usually an essential feature of it. If, therefore, the seller of goods in such a transaction fails to deliver them on time, the purchaser may usually refuse to go ahead. See the case of *Reybold v. Voorhees* (1858), 30 Pa. 116, which was stated in the fifteenth chapter.

(A) The purchaser's right to demand goods of a certain quality.

The purchaser's rights for the most part group themselves around the idea that he should get what the seller agreed to give, in order that the contract may be properly performed. Of course, a contract of sale is, like every other contract, to be performed in accordance with the terms of agreement. While this fact is always true, it is apt to lead to the common mistake that if the buyer is disappointed in the quality of the goods, and finds when he gets them home that they are nothing like what he thought they were, he is at liberty to return them. In general, the law is quite the other way. The contract of sale, according to the general legal principle, is for the passing of title to the article in question,

and if title to that article is passed, the contract is performed and the buyer must be satisfied. He has got what he bargained for, and the mere fact that he thought he was getting something very much better does not form part of the contract. As a rule he may not set the contract aside, even though the seller has praised the article sold up to the skies, and though it turns out afterwards that the praises were all undeserved, and the article is worthless. The courts realize that a great deal of loose talk is indulged in by a man who wants to sell goods, and his puffing up the value of his wares does not ordinarily enter into the contract. The buyer should, therefore, keep before him the maxim, "*caveat emptor*," which means, "let the buyer beware." This legal maxim applies to the ordinary transaction of sale where the parties are dealing at arm's length.

In the case of *Farnsworth v. Wickersham* (1875), 2 W. N. C. 155, a man was sued for the price of a wagon. He defended on the ground that the seller had told him that the wagon was a "first class" one and that it was not really "first class." The court held that the laudatory recommendations of the seller are of no importance and create no legal liability, unless intended and understood to be given as a warranty. It is different where the purchase is made on the faith of the seller's warranting the truth of his statements.

In the case of *Bailey v. Watchhouse* (1876), 3 W. N. C. 275, a man was sued for \$150, the price of a ring. The defendant alleged that he purchased upon the seller's representations that the ring was worth \$150; that it was not really worth more than \$75; that the defendant soon after he got the ring offered to return it; and that the plaintiff knew at the time of the sale that the ring was worth only \$75. It was held that this defense was not sufficient. The buyer is supposed to use his eyes. As the rule is sometimes stated, "the buyer's eyes are his bargain." If the ring had subsequently turned out to be worth \$1,000, the buyer could not have been forced to return it, merely because the seller did not know it was worth so much. The buyer could not set aside the sale because the seller knew more about the ring than he did. A

buyer must rely on his own judgment as a general rule, and if he trusts to the seller's estimate of the value of the article, he must abide by the consequences. The seller is allowed to express freely his opinion of the value of his wares—the buyer is at equal liberty to answer that they are worth nothing. Neither party is bound to communicate that which is equally accessible to both. If the purchaser had no experience in buying such articles he might have called in some expert to assist him in valuing the ring. The seller's commendations of his article were not such as to entrap a reasonably prudent man.

All this does not go the length of stating that a seller of goods is never bound to make good his representations of quality. The buyer has the right under certain conditions to insist that the goods delivered shall come up to the express or implied warranty of the seller as to quality and fitness for certain purposes. It is important to understand, however, that the purchaser must not lightly take it for granted that he can rely absolutely on what the seller says as to the merits of the goods. If the seller has practiced undoubted *fraud* on the buyer, the buyer has a right to set the sale aside. Two Pennsylvania cases illustrate this point. Both related to horse sales. In the first case the seller showed a horse to the buyer and told him that it was a fine, sound horse. The buyer took the horse, but found that it was not sound, and refused to pay the price. The court held him bound to pay, for the seller had not fraudulently concealed the horse's defects. The defects were of a hidden nature, but this fact did not help the buyer. The buyer bought after inspecting the horse and with his eyes open. The seller's statement that the horse was a fine, sound horse did not amount to a warranty of its soundness. A different decision was rendered in the second case. The horse sold was a crib-biter, that is, it had the bad habit of biting at its manger and sucking wind. The seller, in order to conceal this defect, had hitched the horse short, with the rein fastened tightly over the saddle at the time of the sale. The purchaser had inquired why the horse was so hitched, and the seller had falsely answered that it was to prevent his rubbing the saddle.

The element of positive deceit is what distinguishes the latter case from the former one, and the Supreme Court held that in this second case there was such actual fraud as would entitle the purchaser to rescind the sale.

In the first case, the mere general assurance of the seller that the horse was a fine, sound horse was not such evidence of fraud or such a warranty of soundness as would enable the purchaser to disaffirm the transaction.

We must distinguish between the effect of the seller's fraud and the effect of his warranty, for the matters are entirely separate. Looking first at the subject of fraud as perpetrated by the seller, we may lay it down as a general rule that his silence about the defects of his goods, or even his general assurance that the goods are all right, do not amount to fraud. Sometimes, however, the seller stands in such a confidential relationship to the purchaser that the latter is entitled to the benefit of whatever information the seller may have on the subject. Suppose the purchaser has employed a confidential agent to look about for land of a particular kind which is to be used by the purchaser for a certain purpose which the agent knows. The agent owns some land himself, and represents to his principal that he has some land of his own which exactly meets the latter's wants. The purchaser, who has trusted entirely to his agent's judgment, buys the land, and finds later that it is clearly unsuited for his needs. The fiduciary relationship in which that seller stood towards the purchaser would bind him to tell all he knew himself about the suitability of the land for his employer's needs. For further information about setting aside a voidable sale, see the fourth chapter. In that chapter, under the heading "Misrepresentation," a distinction was drawn between misstatements which are made as inducements to the formation of a contract, on the one hand, and warranties, which are actually made part of the contract itself, on the other hand. The misrepresentation may enable the disappointed party to set the contract aside, if he can prove that it induced him to give his consent, and that, therefore, the agreement rested on an unsubstantial foundation. The warranty is part and parcel of the

terms of agreement, and if the person who makes it does not perform accordingly, the other party has a clear case against him.

In the preceding paragraph we have considered the effect of the seller's fraud upon the validity of the contract; we now come to consider what effect the seller's representations as to quality will have on the contract of sale *as a warranty of quality*. We have seen the general rule that there must be an express stipulation that the representations are warranted, in order that they may be binding. The word "warrant" need not be used, but some equivalent form of expression is necessary. Where a buyer intends to rely on the seller's representations, he should be very careful to make the seller warrant the truth of those representations, and here again, as in so many other cases, the importance of getting a written warranty appears. As we have seen in a great many cases, writing is not essential to the validity of a contract, but a written warranty, for instance, helps show the court that the parties really intended to make the warranty part of the contract. Hence they will often give effect to a written warranty, while, if the same words were used verbally, the courts might be disposed to treat them as more or less loose talk on the seller's part in holding up his side of the bargain, and praising the quality of his goods.

Let us consider two more cases in endeavoring to distinguish between what constitutes a warranty and what does not. In the case of *Jackson v. Wetherill* (1822), 7 S. & R. 480, it appeared that the seller of a horse had told the buyer repeatedly that he was sure she was perfectly safe, kind and gentle in harness. The purchaser was satisfied with this assurance, and bought the horse. The court held that the rule of *caveat emptor* will apply with more force to the sale of a horse than any other article. A horse is more the subject of speculative dealing than almost any other chattel and is more liable to secret maladies than most other animals. The purchaser should have secured a definite warranty of soundness and safety. Chief Justice Gibson remarked in a similar case, "if the seller had used expressions *fairly indicating that he was willing to be*

bound by his representations, we might infer that he had intentionally induced the purchaser to deal on that basis, but a naked statement by the seller is not to be treated as a warranty, merely because the purchaser gratuitously relies on it; for the purchaser must be considered foolish had he decided to buy on the seller's judgment, if he fails to exact a direct engagement from the seller as to the truth of the seller's statements." Let us look now at the other side of the line. A seller of leather wrote to a purchaser that his leather had been thoroughly tanned, and the purchaser wrote back, "if your leather is thoroughly tanned now, we will take it." There the purchaser *made his acceptance* of the leather *depend absolutely on the truth of the seller's statement*, and it was held that there was a warranty by the seller that the leather was thoroughly tanned. Again, if an order for slate "strictly No. 1 in quality, and free from gray-backs" is accepted, there is a warranty that the slate shall be of the quality ordered. Again, a representation made by the seller of diamonds that the stones are pure and free from flaws, and that if not as represented the seller will take them back, constitutes a warranty, because the seller's representation was evidently more than a mere loose statement, since the buyer was to have the right to return the goods if not found as represented. The word "warrant" or the word "guarantee" is a good word for the purchaser to insert in the contract, if he wants to hold the seller to make good his representations. Better still, he may insert the clause that "the sale is absolutely conditioned and dependent on the exact fulfilment of the seller's representations." Where the seller tries to substitute an article of an entirely different species from that mentioned in the terms of sale, the question is different from where the dispute concerns merely the quality of the article. If the article is of an entirely different character from that spoken of, it is clearly not delivered in compliance with the contract.

If a defect in the goods sold about which the purchaser complains is such as he must surely have been aware of, he cannot rely on a general warranty of soundness, for it would seem evident that he took the article subject to the defect

which he must have noticed. Where the parties are dealing face to face, and the purchaser has as good a chance to discover the defects in the article sold as the seller, we have seen that it would be unjust to assume that the seller warrants that the article has any particular quality, even if the seller puffs up the merits of his goods somewhat extravagantly. On the other hand, where an article is not in existence at the time the purchaser orders it, it is obvious that the seller should not be allowed to palm off any kind of article which he may make, however imperfectly, in filling the order. In the first case, the purchaser sees the article, and gets what he bargains for; even though he subsequently learns that the article is imperfect. In the second case the purchaser clearly relies, and clearly has a right to rely, on the seller's promise to manufacture a certain article, and the purchaser may well object if the article when made turns out to be different from the seller's representations. Therefore, the courts hold that if an article is ordered from a manufacturer for a particular purpose, and it is made and sold for that purpose, there is an implied warranty, even though the parties have not expressly referred to the matter, that the article shall be reasonably fit for the intended purpose. A manufacturer of machinery is under greater responsibility than a dealer in machinery, for the dealer does not impliedly warrant the quality or fitness of what he sells. The buyer of machinery from a dealer is supposed to buy with his eyes open, and he usually has equal opportunities of observation with the dealer. If a buyer orders a specified article from the manufacturer thereof by its trade name, and the manufacturer makes the known and definite article which goes by that name, it would seem that he has done all that he can be fairly obliged to do. It is doubtful if any warranty of suitability for the buyer's purposes can be implied in such a case.

All these rules are based upon sound reason, and where the reason of a rule does not exist in a particular case, the rule may not be applied by the courts. For instance, if the purchaser is absolutely prevented by the seller from inspecting the goods, the courts will probably reach the con-

clusion that the purchaser must have relied on the seller's representation as to quality, for he was not dealing with him on even terms. Where goods of a particular description are ordered, and the purchaser has had no opportunity to inspect them, there is an implied warranty that the goods shall answer the description and be merchantable in quality; and where the goods delivered are not of the description ordered the purchaser may refuse to receive them. If, however, the purchaser has an opportunity to inspect and neglects to utilize it, the courts are reluctant to allow him to take advantage of his own negligence and to let him claim that he was not on an even footing with the seller, and should have the right to hold the latter to all his representations of quality.

Where a sale of anything is made by *sample*, the act of April 13, 1887, directs that unless the parties agree otherwise, there shall be an implied warranty on the part of the seller that the goods, chattels and property sold and to be delivered are the same in quality as the sample shown. The act of May 4, 1889, directs that in every sale of green, salted, pickled or smoked meats, lard and other articles of merchandise, used wholly or in part for food, said goods or merchandise shall correspond in kind and quality with the description given by the seller; and in every sale of such goods, unless the parties shall agree otherwise, there shall be an implied contract that the goods are sound and fit for household consumption.

(B) *Warranty of the purchaser's title.*

A very important warranty which is implied in sales of personal property is the warranty of title. The word "implied" means that the party who makes the sale, even though he does not declare that he is the owner and has a good title, does actually under the law give the purchaser a silent warranty that he has a right to sell the article. If he has no right at all, the purchaser may recover the money which he has paid. If there is a lien against the article, of which the seller did not inform him, he has a right to insist **on the seller's** paying off the lien. One exception to this rule of implied warranty is generally recognized in the case of

official sales. Suppose the seller acts in the capacity of sheriff, administrator, executor, guardian or trustee in bankruptcy. In making sales such a seller does not stand in the attitude of the owner, but sells the right of another. While he may, if he chooses, expressly warrant that he is passing title, it is held that there is no implied warranty. Another exception occurs where the seller disposes of his "right, title and interest" in certain goods. In such cases he is not undertaking absolutely to sell the goods, but merely to give a quitclaim covering any property rights which he may possibly have in them.

PART III

LEASES OF REAL PROPERTY

CHAPTER XLIV.

THE FORMATION OF THE RELATION OF LANDLORD AND TENANT.

We have considered certain contracts relating to personal property in the preceding parts of this book. In the first part we studied bailments. When a bailment is made the possession of personal property is delivered to the bailee, but the ownership is not transferred to him. In the second part we studied sales of personal property. When a sale is made, the title is transferred to the purchaser, but he may or may not receive actual possession. A similar distinction may be drawn between leases of realty, which are treated in this third part, and sales of realty which will be dealt with in the fourth part. When a lease is made, the lessee usually gets personal possession of the leased premises, but not the absolute ownership and title. When a valid sale of realty is made, the purchaser gets title, but he may or may not go into immediate personal possession.

Certain long leases require special formality, as will be seen later in this chapter, but a short contract of lease may be made either by conduct, by word of mouth or by writing. We shall consider these three methods of forming the relationship of landlord and tenant in the order named.

(A) Contracts of lease implied from the conduct of the parties.

In the second chapter under the third rule we saw that offer and acceptance need not be made by words but may simply appear from the actions of the parties. This applies to the relation of landlord and tenant. The owner of land

may recover compensation from the person who has occupied it, where the situation is such that an agreement to pay rent may fairly be implied. In the case of *Henwood v. Cheeseaman* (1817), 3 S. & R. 500, the court held that if the defendant, who was sued for rent, had occupied the land with the owner's permission, the jury might infer a contract to pay a reasonable sum for the use of it. The land in question was located in New Jersey, and the alleged tenant complained that suit should not have been brought before a Pennsylvania court. It was decided, however, that a contract, whether express or implied, gives rise to a personal relation between the parties, and the one who breaks it may be sued for damages wherever he can be personally served with a summons.

In the case of *Sterrett v. Wright* (1856), 27 Pa. 259, the owner of land sued his son-in-law on an implied contract to pay rent. The court held that when one person receives anything of value from another, the law implies a promise that he will pay what it is worth. This rule has its exceptions. A son, for instance, cannot charge for labor bestowed about his father's business, and a parent cannot recover for the maintenance of his child without distinct and clear proof of an agreement to pay. Where a son occupies his father's land, without promising to pay rent, the law does not imply an agreement on his part to do so. There is a natural presumption that the immediate members of the same family are not benefiting each other with the expectation of pecuniary rewards. No contract can be implied to pay for those things which it is the universal custom to give gratuitously. A person who stops at an inn is liable to suit if he does not pay his bill; but one who visits his relative incurs no obligation to pay for his entertainment. The court stated, nevertheless, that it is not customary for men to occupy the lands of their fathers-in-law without paying rent. The burden of proof fell upon the son-in-law to show that his use of the land was intended to be gratuitous. The relationship, however, is a circumstance to which the jury should allow its proper weight. The condition in life of the parties may also render it easier for the defendant to make out his case. If his

father-in-law had been a millionaire, and he had been without means himself, this would make the son-in-law's contention that he was not expected to pay rent more plausible. The evidence that the use of the land was given gratuitously needs to be strong only in proportion to the natural improbability of the contention.

In the case of *Spackman's Appeal* (1884), 16 W. N. C. 79, it was held that where a niece occupies her uncle's land, there is an implied obligation to pay rent, despite the relationship. The circumstances of a particular case may rebut this inference. In the case of *Overseers v. Overseers* (1892), 148 Pa. 1, a different conclusion was reached where the same relationship existed between the alleged landlord and tenant. It appeared that a man had lived with his uncle as one of the same family. He had no distinct possession of any portion of the uncle's house. His work went to help keep the entire family. The court said that a lease cannot be fairly implied from circumstances and conduct which show that none was intended by the parties. All contracts grow out of the intention of parties to transactions, and are dictated only by their mutually accordant wills. When this intention is expressed, we call the contract an expressed one. When it is not expressed, it may be inferred, or presumed, that is to say *implied* from circumstances as really existing. And the contract thus ascertained is called an implied one. In the case of *Bardsley's Appeal* (1887), 20 W. N. C. 90, it was held that a prospective purchaser of land who goes into possession under a contract that title shall be conveyed to him cannot usually be presumed to be a lessee. It is customary, where a prospective purchaser takes possession of the land before he makes settlement, to have him sign a lease. If the contract of sale falls through, the owner is in a much better position to deal with the party in possession, than if no lease had been made.

(B) *Leases by word of mouth.*

A verbal lease is legally valid, unless it falls within the act of March 21, 1772. This statute was treated at length in the seventh chapter. It requires all leases for over three years from the making thereof to be in writing and signed

by the landlord or by his agent. Where the agent signs, his authority to do so should appear in writing. Where a lease for over three years is made by word of mouth, it has the effect of merely a lease at the landlord's pleasure. Suppose the parties verbally agree that the tenant shall be allowed to remain in possession for ten years, and pay a certain rent during that time. Neither of them can compel the other to fulfil this unwritten agreement.

A verbal lease for three years is good, but the term of three years must be computed from the time when the agreement was made. Suppose the tenant is not to go into possession of the premises for a year from the date of the agreement. If the term fixed by the agreement is more than two years, the act of 1772 will apply to it. *Only the lessor's signature is required by the statute*, so that if the tenant accepts the lease he is bound by all its terms, provided the lessor signed it. It was noted in the seventh chapter that the courts will sometimes enforce a verbal contract in spite of the statute, in order to prevent great injustice. Thus in the case of *Witman v. Reading* (1899), 191 Pa. 134, it is said that if a tenant makes extensive improvements on the faith of the landlord's verbal promise to lease the premises for over three years, the latter will not be allowed to take advantage of the statute.

No land-owner should make even a short lease by word of mouth, because the ordinary printed or written forms of lease contain many terms which cannot be conveniently mentioned in a verbal agreement. The advantages of written over verbal contracts, as explained in the eleventh chapter, are particularly apparent in this matter of leases. In the specimen form of lease given later in this chapter, you will note several drastic legal remedies which are designed to protect the landlord in case of trouble.

(C) *Written or printed leases.*

It makes no difference whether the terms of a lease are written or printed, for they are presumed in either case to express the intention of the parties. Both parties should sign the contract, which should be executed in duplicate. The

tenant should insist on receiving a copy of the contract, executed in precisely the same way as that which the lessor gets. Some landlords unfairly attempt to deny their tenants copies of the lease. Even if a tenant insists on getting a copy, these landlords will try to satisfy him with an unsigned copy or a signed one marked "duplicate," while the landlord's copy is marked "original." It is better to have both copies exactly the same in all respects.

Where a lease is for more than twenty-one years, it should be recorded in the office of the Recorder of Deeds of the county where the land lies. In order that it may be admitted to record, it should be acknowledged before a notary or other official authorized by the law of Pennsylvania to take acknowledgments to deeds. Suppose that John Smith is the landlord, and is leasing for thirty years. The following form of acknowledgment may be recommended:

"On this third day of September, A. D. 1906, before me, a notary public of the Commonwealth of Pennsylvania, for the County of Lackawanna, personally appeared the above named John Smith, and in due form of law acknowledged the above lease to be his act and deed, and desired the same might be recorded as such."

As the agreement between landlord and tenant may vary in a thousand particulars, so the terms of a lease must be drawn to correspond with their intention. The following form of lease, however, contains a number of terms which suit the requirements of most cases:

THIS AGREEMENT WITNESSETH, That Thomas Bright, hereinafter called the lessor, hereby lets unto James Finn, hereinafter called the lessee, the factory, with the yard in the rear thereof, located at numbers 500 and 502 Mulberry Street, Lancaster, for the term of three months from the first day of October, A. D. one thousand nine hundred and six (1906), at the rent of one hundred dollars (\$100) per month, to be paid monthly in advance, the first payment thereof to be made on the first day of October, A. D. 1906, and said lessee hereby agrees to pay said rent to the said lessor on the days and times aforesaid, at 316 Court Street or at such other place within Lancaster as said lessor may in writing from time to time direct, without demand being made therefor, and to pay within ten days after the same shall become due and payable all bills for gas consumed in or

on said premises during the continuance of this lease, and after that time, until the flow of the same is stopped by the proper authorities, and that he will not assign this lease, nor underlet the said premises, or any part thereof, or use or occupy the same other than as a factory for the making of cigars and other tobacco goods, without the written consent of the said lessor first had and obtained, and during the said term will keep said premises in good condition, order and repair, will remove, or cause to be removed, any and all ashes, rubbish or refuse matter therefrom, and at the termination of said term will deliver up the said premises in as good condition, order and repair as the same now are, reasonable wear and tear, and damage by accidental fire excepted. The lessor shall have the right to display a "For Sale" sign at any time, and also, after notice from either party of his intention to determine this lease, a sign "For Rent" or both "For Sale" and "For Rent," in a conspicuous place in front of the premises. The lessee shall permit said premises to be examined by any person or persons upon an order from the lessor. And the said lessee further agrees that if the rent shall remain unpaid on any day on which the same ought to be paid, then the lessor may enter the premises, and proceed by distress and sale of the goods there found, to levy the rent and all costs and officer's commissions, including the five per cent chargeable by Act of Assembly to the lessor. The said lessee further agrees that all goods on the said premises, and for thirty days after removal, shall be liable to distress for rent, and hereby waives the benefit of all exemption laws in relation thereto. And said lessee further agrees that this waiver shall extend and be applicable to any process, execution or executions that may be issued in any and all suits, actions or proceedings, for the collection of rent due and in arrear, for any gas bills left unpaid, for any expense incurred in removing ashes, rubbish or refuse matter from said premises, and for damages for the non-fulfilment of any of the covenants herein contained. Upon the total destruction of the premises by fire or other casualty, this lease may be terminated by either party by giving two days' written notice to the other. And it is hereby mutually agreed that either party hereto may determine this lease at the end of said term of three months by giving the other notice thereof, at least thirty days prior thereto, but in default of such notice, this lease shall continue upon the same terms and conditions as are herein contained for a further period of three months, and so on from month to month, unless or until terminated by either party hereto giving to the other thirty days' written notice for removal previous to the expiration of the then current term. *Provided, however,* that if the lessor shall have given thirty days' written notice previous to the expiration of the said term, or any extension or renewal thereof as above, of his intention to change the terms and conditions of this lease, and the lessee shall hold over after such notice he shall be considered lessee under the terms and conditions mentioned in such notice, for such further period as he may remain in possession of said premises, and

until this lease is terminated by notice as hereinbefore provided. And it is further agreed that if the said rent shall at any time be in arrear and unpaid, or if the said lessee shall underlet or otherwise use the said premises than as above expressed, or shall fail to comply with the conditions of this lease, or notice given under the terms thereof, or shall not well and truly perform and fulfil all and every the covenants and agreements herein contained on the part of the lessee to be performed and kept, then this lease shall, at the option of the said lessor, cease and absolutely determine, and any attorney may immediately thereafter, as attorney for the said lessee, at the sole request of the said lessor, sign an agreement for entering in any competent court, an amicable action and judgment in ejectment (without any stay of execution or appeal) against the said lessee and all persons claiming under said lessee for the recovery by the said lessor of possession of the hereby demised premises, without any liability on the part of the said attorney, for which this shall be a sufficient warrant; and thereupon a writ of *habere facias possessionem* may issue forthwith without any prior writ or proceeding whatsoever, and the lessee hereby releases to the lessor all errors and defects whatsoever in entering such action or judgment, or causing such writ of *habere facias possessionem* to be issued, or in any proceeding thereon, or concerning the same; and hereby agrees that no writ of error or objection or exception shall be made or taken thereto; and a copy of this lease, verified by affidavit, being filed in said action, it shall not be necessary to file the original as a warrant of attorney, any law or rule of court to the contrary notwithstanding. No such determination of this lease, nor taking or recovering possession of the premises, shall deprive the lessor of any other action against the lessee for possession, for rent, for any gas bill left unpaid, for any expenses incurred in removing ashes, rubbish or refuse matter from said premises, or for damages. All rights and liabilities herein given to, or imposed upon either of the parties hereto, shall extend to the heirs, executors, administrators, successors and assigns of such party.

IN WITNESS WHEREOF, the said parties have hereunto set their hands and seals, this third day of September, one thousand nine hundred and six (1906).

[Signed]	THOMAS BRIGHT, (Seal)
[Signed]	JAMES FINN. (Seal)

Sealed and delivered in
the presence of
[Signed] HENRY DUKE,
[Signed] MARTIN LEARY.

Frequently a landlord insists upon his tenant's furnishing a surety, and the following is a form of surety contract by which Francis Miller becomes responsible for the perform-

ance by James Finn of the terms of the foregoing contract of lease:

I, Francis Miller, hereby agree to be responsible to the within-named lessor or his assigns, for the true and faithful performance of the within contract on the part of the within-named lessee and hereby waive the benefit of all laws made or to be made, exempting any of my property from levy and sale under execution or any part of the proceeds arising from the sale thereof, from the payment of any judgment obtained hereon.

IN WITNESS WHEREOF, I have hereunto set my hand and seal, the third day of September, one thousand nine hundred and six (1906).

[Signed] FRANCIS MILLER. (Seal)

Sealed and delivered in

the presence of

[Signed] PETER MILLER.

[Signed] JOHN GROOME.

An explanation should be made here of some of the terms of the form of lease given above. In the next two chapters the reason for inserting many of these terms will appear, as the rights of the landlord and tenant are taken up in detail.

The terms providing for the ejectment of the lessee are important, because when you put a tenant in possession of your property, you give him a certain legal standing. It is difficult to evict him promptly, if he breaks the terms of a lease, unless you have a strong ejectment clause. The clause by which the tenant waives the benefit of the exemption act of April 9, 1849, is desirable, for without it he could hold \$300 worth of property, and all his wearing apparel and that of his family, as well as a few other articles free from the landlord's claim. The clause forbidding an assignment is inserted because the tenant might assign the lease if there were no such clause.

The following additional clauses are sometimes inserted in leases. The form given above may be varied by adding some or all of them:

"The lessee will permit the lessor or his duly authorized employees to enter the premises at all times, if the lessor shall in his free discretion so desire, for making repairs, alterations or additions to the premises. The lessee further agrees at his own cost and expense to comply with and perform

any and everything as may be required under notice from any of the constituted authorities. The lessee shall not erect or cause to be erected any sign without the written consent of the lessor. If the lessee shall become embarrassed, make an assignment for the benefit of creditors, be declared a bankrupt, voluntarily or involuntarily, or if the lessee's personal property shall be sold by sheriff's or marshal's sale, then the rent for the said term, or any term or balance of any term hereby created, shall at once become due and payable as if by the terms of this lease it were all payable in advance, and shall be first paid out of the proceeds of such assignment, bankrupt estate or sale, any law, usage or custom to the contrary notwithstanding. The lessee shall not place weights in any portion of the demised premises beyond the safe carrying capacity of the structure. The lessee shall not do or commit, or suffer to be done or committed, any act, matter or thing whereby, or in consequence whereof, the policy or policies of insurance on the said premises, or any part thereof, or on the building of which the demised premises may be a part, shall become void or suspended, or whereby or in consequence whereof the insurance risk on said premises, or any part thereof, or on the building of which said premises may be a part, shall be rendered more hazardous than at the date of the execution of this lease, and the lessee will pay as rent any increase of premium caused by reason of the breach of this covenant, and *in the event of the total destruction by fire, or total destruction by other casualty, the rent shall cease from the date of such fire or other casualty, and possession of the premises shall be surrendered by the lessee to the lessor.* The lessee further agrees that no explosive materials of any kind shall be kept in or about said premises. The lessee further agrees to pay, as rent, any additional charges that may be assessed by the proper authorities for the use of water over and above the rate of record at the date of the execution of this lease. No alterations or improvements to the said premises shall be made without first having the consent in writing of the lessor, and any improvements or alterations made by the lessee after such consent shall have been given, shall become the property

of the lessor, and shall remain, or be removed at the lessee's cost, at the expiration or other sooner determination of this lease, as the lessor may elect. The lessee agrees that the lessor shall not be held responsible for, and is hereby especially relieved from, any liability by reason of damage or injury to persons or goods caused by any break or leak in any part of these demised premises or in the pipes or plumbing work of the same, or from any other place or quarter, or that may be caused by the acts of any person or persons whether representing the lessor or otherwise. If the said lessee shall at any time during the continuance of this lease, attempt to remove or manifest an intention to remove the goods and effects out of or off from said premises without having paid and satisfied the lessor in full for all rent which shall become due during the term of this lease, or any renewal thereof, then and in such case, such removal or attempt to remove, shall be considered fraudulent, and the whole rent for the whole term of this lease, or any renewal thereof, shall be taken to be due and payable; and the said lessor may proceed by landlord's warrant or other process to distrain and collect the whole in the same manner as if by the conditions of this lease the whole rent were payable in advance. If the said lessee shall remove from the premises during the said term, or any renewal thereof, or cease to use or occupy the same as herein provided, the lessor in his discretion may immediately and without liability therefor, re-enter said premises by force or otherwise, without notice or demand, and lease the said premises to any other person or persons, and the said lessee shall be liable for any loss in the rents for the balance of the then current term."

The clause providing that the tenant's liability for rent shall terminate if the buildings on the premises are destroyed by fire or otherwise should usually be insisted on by the tenant. Without this clause he is bound to continue paying rent even though the buildings are burned down at the very beginning of his term. The rule that the destruction of a building by fire does not release the lessee from liability for rent cannot be applied to a lessee who rents an apartment in a building. *Parson & Comfort Co. v. Potter* (1906), 30

Super. 615. A fire clause is included in the long form of lease at the beginning of this subdivision.

The tenant should be careful to see that the lease is signed by the real owner of the property. If he accepts a lease from a real estate agent, it may be that the latter is acting for another tenant who wants to dispose of his lease. If the first tenant has not paid his rent, the goods of the second tenant, who is called a sub-tenant, which he has on the leased premises will be liable to seizure by the landlord. In the following case we shall notice that a sub-tenant's goods are liable to distraint for rent due by the main tenant.

Whiting & Co. v. Lake (1879), 91 Pa. 349, shows the danger which a tenant runs if he fails to get a lease from the owner. Henkle & Brother rented a storeroom belonging to Mrs. Simpson in Pittsburgh, and Whiting & Co. took possession of the premises during Henkle & Brother's term, shortly after Henkle & Brother had discontinued business. At the time Whiting & Co. took possession there was a sign in the window reading as follows: "To Let. Inquire at 177 Penn Avenue, or of D. F. Pennington, Room 7, upstairs." Whiting & Co. called at 177 Penn Avenue, where they found Mrs. Simpson's brother. He declined to rent the storeroom in the way desired by Whiting & Co., telling them to see Dr. Pennington, who, he said, might make the desired arrangement. Dr. Pennington had a room in the building where the storeroom was, and had a sign on the door of the hallway marked, "D. E. Pennington, agent for this building." Pennington rented the storeroom to Whiting & Co. Later, on April 1, 1875, Whiting & Co.'s goods in the storeroom were seized by the sheriff, Bennett Lake, for \$500 rent due by Henkle & Brother. Mrs. Simpson, it was testified, never gave Pennington authority to lease the storeroom, but merely authorized him to try to direct a suitable tenant to her for her approval. Pennington collected the rents of the second and fourth floors, and was authorized to lease rooms on these floors, for which he held a power of attorney defining his authority in the matter.

The court held that Pennington's action, which Mrs. Simpson had not authorized, failed to bind her. If Whiting

& Co. went into possession under Henkle & Brother, and held over after the termination of Henkle & Brother's lease, or if they were in without authority from anyone, their goods on the premises were liable to be distrained for rent due by Henkle & Brother.

Where a tenant is to pay for expensive improvements to the premises, he should be specially careful to make sure that he is renting from the real owner. Some real estate agents make a practice of drawing up their leases without naming the real owner of the premises. If Philip Baker owns the house, and John Smith is the agent, the lease will recite that it is made by "John Smith, Agent." Such leases frequently provide that the agent shall not be held personally responsible, and the tenant is put at a great disadvantage. If you are to become a tenant under an improvement lease, you may find it wise to have the title to the premises searched. Insist upon the real owner's signing the lease. Perhaps you will find the property so heavily mortgaged as to make you fear lest the present owner should lose control of it. If the property is sold at sheriff's sale for non-payment of the interest or principal of the mortgage, the purchaser is not bound to allow you to remain in possession, if the mortgage was made prior to your lease. If, however, the landlord sells the property himself, either at private sale or public auction, to a third party, the latter is bound by the terms of the lease.

CHAPTER XLV.

THE LANDLORD'S RIGHTS.

The chief object that the landlord has in view is usually that of obtaining *rent*. Unless the lease provides otherwise, rent is payable at the end of the term for which it is made. If, however, the conduct of the parties shows an understanding that the tenant should pay by instalments, he would be bound to do so. *Ellis v. Rice* (1900), 195 Pa. 42. Landlords usually insert a provision for the payment of rent either

at the beginning of the term or, periodically, at the beginning of every month or quarter or year. Rent, like most other debts, carries interest from the time it falls due. Most leases provide that the rent shall be payable at whatever place the landlord may designate; otherwise, it is payable on the leased premises, and the landlord is bound to come there for his money.

In addition to the landlord's right to sue for the rent, he has the right to *distrain*. This right enables him when the rent is in arrears to enter the premises and seize such goods as are liable to distress. These include furniture, farm produce and nearly every kind of goods of a tangible nature. They do not include such intangible property as a license to sell liquor on the premises which the tenant may enjoy. If the tenant agrees in a lease to pay taxes assessed on the premises, and fails to do so, the landlord may distrain, because the agreement to pay taxes is in the nature of a promise by the tenant to pay rent. A distraint may be made the day after the rent falls due, even though it is payable in advance. In the preceding chapter it was mentioned that the act of April 9, 1849, secures a certain exemption to a tenant; and this act may enable a tenant who has no valuable property to defeat the distraint, unless he has waived the right to claim his exemption.

In addition to the tenant's own property, that of his wife is liable. Likewise, the goods of a sub-tenant, although the latter has paid his rent to the principal tenant. The sub-tenant's goods are liable even though the landlord has declined to recognize the sub-tenancy, and though the main tenant has enough goods on the premises to answer the landlord's purposes. The danger which a sub-tenant runs is shown in the case of *Whiting & Co. v. Lake* (1879), 91 Pa. 349, set forth in the preceding chapter. The goods of a stranger upon the premises are also liable, *unless they have been placed there in the course of the tenant's trade or business*. Thus cattle or horses sent by their owner to the tenant, in order that he may let them graze on a leased field, are not distrainable, where the tenant receives hire for pasturing them. *Cadwallader v.*

Tindall (1853), 20 Pa. 422. Goods stored with a warehouseman in the ordinary course of business, or consigned to a commission merchant are not distrainable. On the contrary, if the goods are not in the tenant's possession by way of trade, but he has taken charge of them as a matter of favor, the landlord may seize them on account of rent.

If the tenant takes in *boarders*, who are admitted into the family circle, and get meals from the boarding house-keeper, such of their goods as they actually use are not distrainable. The goods of a *sub-tenant* or a *renter of rooms* are not exempted, but a boarder's goods in use by him are deemed to be on the premises in the course of the tenant's business. *Riddle v. Welden* (1839), 5 Wharton 9. Goods in the custody of the law are not distrainable. For instance, where the tenant's goods have been seized under an attachment, the landlord cannot take them, but he is entitled to a priority out of the proceeds of such goods when sold in legal proceedings, for rent due at the time the sheriff attached them, not exceeding one year's rent. If the tenant goes into insolvency under the Pennsylvania act of 1901, or into bankruptcy under the national act of 1898, his goods on the premises are subject to the same priority claim. The landlord may assert this claim out of the proceeds of such goods, but he has no priority as to the proceeds of goods which have not been on the premises, since he never had a lien on them.

The act of May 13, 1876, provides that pianos, melodeons and organs leased or hired to the tenant shall be exempted from distress, provided that the owner of them, or his agent, gives notice that they are leased or hired to the landlord, or his agent, at the time of the leasing or hiring. The act of June 25, 1895, makes a similar provision for sewing and typewriting machines. The act of April 28, 1899, makes a similar provision for soda water apparatus leased or hired to the tenant.

The act of March 21, 1772, directs that if any tenant fraudulently or secretly removes goods from the premises in order to prevent the landlord from distraining on them, the latter may follow them, and seize them wherever found, pro-

vided he does so within thirty days after such removal. If, however, they have been sold before the seizure to innocent third persons, for a valuable consideration, the latter are protected. In most written leases, a clause is inserted permitting the landlord to seize any goods removed from the premises within thirty days after such removal. This does not affect the rights of *bona fide* purchasers for value, but it spares the landlord the necessity of proving that the goods were removed fraudulently or secretly and in order to defeat his rights.

After the landlord or his agent, who is usually a constable, has seized the goods, the act of March 21, 1772, provides that the tenant shall have five days' notice before further proceedings are taken. This notice is given in order to allow him a chance to pay the rent or to prevent further action if the distraint is illegal. Suppose, for instance, that no rent is actually due. The tenant may take proceedings to recover his goods by an action of replevin. A replevin suit halts the distraint proceedings, and the tenant gives a bond to satisfy the landlord's claim, in case the outcome of the replevin suit should show that the rent was really due. Let us assume that the tenant does not bring a replevin suit. After the five days are up, the person who makes the distraint should have the distrained goods appraised by two reputable persons. The appraisers must first take an oath or affirmation to make the appraisement well and truly, according to the best of their understanding. The sheriff, deputy sheriff or constable administers the oath or affirmation. When the appraisement has been made, a public sale of the goods may be held after six days' public notice. See the case of *Whitton v. Milligan* (1893), 153 Pa. 376. The proceeds of the sale, which should be conducted publicly, go toward paying the arrearages of rent and the costs of the distraint. The balance, if any, should be returned to the tenant. The act of March 21, 1772, provides a penalty for distraining when no rent is in arrears. The tenant may recover double the value of the goods sold, together with full costs of suit. If the tenant unlawfully rescues his goods after they have been distrained, he is liable to the injured party for treble damages, as well as the costs of suit.

Besides suing on the contract of lease for his rent, in case it is not paid, or distraining for it, the landlord has the right to *eject* the tenant. This is a troublesome and tedious proceeding unless the lease provides a speedy method for ousting the tenant. The form of lease given in the last chapter contains the proper terms for the landlord's protection in this respect. The act of March 31, 1905, provides that where the tenancy is for any time less than one year, or by the month, or for an indeterminate time, the immediate landlord or the owner may make written demand for possession within thirty days. The tenant cannot, however, be dispossessed before the expiration of his license or lease. The act of April 10, 1905, provides for the forcible breaking into the premises by a constable, where the tenant wrongfully and forcibly withholds possession.

Most forms of leases contain a provision regulating the continuance of the tenant upon the premises after the term fixed. This provision usually recites that if neither the tenant nor the landlord shall give the other notice of intention to discontinue the lease, it shall be extended automatically for a further named period. If there is not such a clause, the landlord has the choice of treating a tenant who holds over either as a trespasser or as a tenant from year to year. If the landlord does not proceed to remove the tenant, and accepts rent from him, it is taken for granted that the terms of the old lease still apply, so far as they are consistent with a lease from year to year. In the case of *McCanna v. Johnston* (1852), 19 Pa. 434, the lease had no provision for a further term, after the period fixed, and expressly provided that the tenant should deliver up possession at the end of the original term without further notice, and that the landlord might enter upon the premises at the end of the period, or at any time thereafter. The tenant held over after his term expired, and the landlord permitted him to remain in possession for many months subsequently, and then started ejectment proceedings. The tenant contended that the landlord's omission to oust him promptly made him a tenant from year to year, and gave him a right to expect a three months'

quit-notice before being dispossessed. The court held that the strict terms of the lease mentioned above relieved the landlord from the duty of serving any quit-notice, and gave him the right to institute the ejectment suit, even after a long delay.

A tenant should be careful to vacate premises before the expiration of his lease, when he does not intend to hold over. If he has a sub-tenant, he should see that the latter also moves out on time. A holding over by a sub-tenant will bind the principal tenant for another term, if the landlord so chooses. What has just been said about a tenant's continuing on the premises after the term expires applies also to cases where the landlord has served a quit-notice. There is this difference, however, that the tenant under these circumstances is not free to consider himself as a tenant from year to year, unless the landlord actually agrees to this, expressly or by conduct. The omission by the landlord to take measures for ousting the tenant during an entire year after the latter begins to hold over does not, in view of the quit-notice, destroy the landlord's right to start immediate ejectment proceedings.

When the landlord sells the leased premises, the purchaser is bound to take notice that they are occupied by a tenant. A private sale or an unofficial auction sale cannot defeat the tenant's rights. The purchaser should demand an assignment of the lease to him, and should promptly notify the tenant that he has bought the property. Usually an agreement of sale provides for an apportionment of the rent as of the date of settlement. Suppose that the tenant is in upon a monthly lease, and has paid a month's rent in advance on September 1, 1906. If settlement is made on September 15, an apportionment would compel the seller to give the buyer credit for half a month's rent. If, however, the agreement of sale is silent on this subject, the rent cannot be apportioned. It belongs to the person who owned the property on the day it fell due. In the case suggested, the seller would be entitled to the entire rent due September 1, 1906, even though the tenant failed to pay it until, say, September 20, if the sale was made subject to the lease.

CHAPTER XLVI.

THE TENANT'S RIGHTS.

The main right obtained by a tenant is to be allowed to enjoy peaceful and uninterrupted possession of the leased premises. In *Mqule v. Ashmead* (1853), 20 Pa. 482, suit was brought for the breach of a verbal lease for five years. The tenant had gone into possession, and had improved the property at great expense. At the end of three years he was turned out through certain Orphans' Court proceedings. The court allowed him to recover damages for his loss, for the word "lease," like the word "demise," implies a promise by the landlord that the tenant shall enjoy the premises in peace during the term fixed. The improvements which the tenant had made brought him out of the operation of the act of 1772, requiring leases for over three years to be in writing. Even though the landlord desires to have the tenant remain in possession, but the latter is evicted by some one who has a better title than that of the landlord, he must pay the tenant damages for breach of contract.

The tenant's right to enjoy peaceful possession of the premises is infringed by any interference with the tenant which practically amounts to an eviction. In the case of *Doran v. Chase* (1876), 2 W. N. C. 609, suit was brought by a landlord upon a five years' lease. The lease did not forbid sub-letting, and the tenant had sub-let to different persons for two years. The landlord told the tenant, as well as several of the sub-tenants, that if any more sub-letting was done, the rent derived therefrom must be paid to him, or he would sue for it. The tenant left the premises on account of these threats. When he was sued for subsequent rent, the court instructed the jury that if the landlord had been the means of preventing the tenant from sub-letting, he could not, under the circumstances, recover. The jury found in the tenant's favor, and the Supreme Court affirmed the judgment. In the case of *Hoeveler v. Fleming* (1879), 91 Pa.

322, Hoeveler sued for certain rent which she claimed was due under a five years' lease. The premises had been rented in April, 1873, and the buildings were made untenable by fire in March, 1877. The tenants, Fleming & Co., had agreed to deliver up the property at the end of the term in good repair, "reasonable wear and tear and accidents by fire excepted." It was explained towards the end of the forty-fourth chapter that a tenant under these circumstances is usually bound to pay rent after a fire occurs, unless there is a provision expressly releasing him from liability. The term quoted above frees him from any obligation to restore the burned premises to their former condition, but it does not suspend the rent. Fleming & Co., however, were excused from paying rent, because Hoeveler had re-entered the premises, and rebuilt them.

This case deserves careful thought. If Hoeveler had been content to let the building stand, roofless and scarred by fire, until the five years were up, she could have recovered all the rent from Fleming & Co. Instead, she, or the fire insurance company for her, took possession of the premises. If this had been done with the consent of Fleming & Co. it would at most only have suspended the rent, while the repairs were being made. As it was done without their consent, it amounted to an eviction, and terminated the lease entirely.

How far the entry of the landlord to make repairs will work an eviction must depend to some extent upon the circumstances of each particular case. When the landlord is bound by the lease to make repairs, and the repairs are **merely** such as are required by ordinary wear and tear, no difficulty is likely to arise. Where he is not bound to make repairs, he should never make them without getting the tenant's consent. It is wise to have a term in the lease authorizing the landlord to repair the premises at any time, if he may choose to do so. In case the landlord wilfully evicts the tenant from a portion of the premises, the latter may treat the entire lease as having been terminated.

The tenant cannot force the landlord to make repairs, unless the latter has agreed to do so. Neither may the tenant

have them made himself, and deduct the cost from the rent. The same rule applies where the property becomes untenable and dangerous, and unfit for carrying on the tenant's business. See the case of *Huber v. Baum* (1893), 152 Pa. 626. The mere fact that the landlord has previously made repairs of a certain kind does not bind him to continue doing so. It would seem that where the landlord authorizes repairs of a permanent nature, and the tenant has them made, the landlord is liable. He is the owner of the property, and such repairs substantially benefit it. *Cornell v. Vanartsdalen* (1843), 4 Pa. 364. The landlord is not bound to have the premises in tenantable condition for the tenant, when the latter takes possession. There is no implied agreement that the property shall be suitable for the purpose for which it is rented. Nevertheless, in the case of *Wolfe v. Arrott* (1885), 109 Pa. 473, the court stated that where a lease stipulates that the tenant shall not use the premises leased save as a dwelling house, there is an implied representation that the house shall be in all respects fit for human habitation. Arrott sued Wolfe for rent, and the latter proved that the drainage on the premises was extremely defective. As this nuisance had existed at the time Wolfe took possession, he was justified in employing a plumber to remedy the drainage, and in deducting the amount of the plumbers' bill from the rental. The landlord is under no duty to tell the tenant that the premises have a bad reputation, or that an adjoining owner is about to build a wall which will keep light and air away from a part of the leased premises. In general, the rule is that the tenant must make the lease with his eyes open, for the parties deal at arm's length. The landlord is not in the position of a trustee or other fiduciary, and is not usually bound to reveal anything to the tenant. *Hazlett v. Powell* (1858), 30 Pa. 293. See, however, *Wein v. Simpson* (1856), 2 Phila. 158.

Unless the lease provides otherwise, a tenant is legally liable to make ordinary repairs, to prevent the premises from falling into decay. For instance, he should remove at his own expense slight obstructions in the drain pipes, which do not entail heavy plumbers' bills. He is not bound to make substan-

tial and extraordinary repairs such as to put on new roofing. Neither may he be compelled, without a specific agreement, to restore premises which have been burned down or otherwise destroyed by an accident, unless it has been due to his negligence or malice. If he chooses to put permanent repairs on the leased property without the consent of the landlord, the latter cannot be charged with them.

Where there are several tenants in the same building, they must exercise their rights in a reasonable manner. The common staircases should not be obstructed by any of them to the detriment of the others.

In one case a second floor tenant was forbidden by an injunction from keeping the front door locked during the daytime. Where the building is used for business purposes, it would seem that the ground-floor tenant has no right, in the absence of a specific agreement, to prevent the upper tenants from displaying their signs and showcases about the entrance way. *Cunningham v. Entrekin* (1894), 3 D. R. 291.

The subject of *fixtures* has caused considerable litigation. The general rule is that whatever permanent improvements are made by the tenant belong to the owner of the property, and must not be removed. An important exception to this rule is made in the case of fixtures fastened to the premises by the tenant in the course of his trade. Moreover, where a tenant puts in fixtures or conveniences for his own comfort, the law raises no presumption that he intended them as permanent improvements, to be left for the benefit of his landlord. As a general rule he will be entitled to remove them during his term. If the removal injures the landlord's property, the tenant is, of course, liable for damages. When, therefore, a tenant removes fixtures, he should be careful to do it before the expiration of his term, and to restore the property to its former condition.

The question as to whether fixtures are removable or not, depends largely upon the intention with which they were set up. In the case of *Jermyn v. Dickson* (1874), 3 Luz. L. R. 100, the dispute concerned the tenant's right to remove a certain pump. The landlord had leased a mine to him, and

the tenant had agreed to make all necessary repairs and improvements at his own expense, including the installation of a pump. Nothing was said in the lease about the removal of these improvements or the tenant's right to demand compensation for them. The court held that the parties must have intended that the pump should remain in the mine. Great damage would have resulted from its removal, and the court seemed to think that the parties would have stipulated for its removal or for compensation to the tenant, unless the cost of putting it up was regarded as virtually part of the rent he had to pay. *Ordinarily, however, trade fixtures are removable, and title to them remains in the tenant*, unless he abandons them upon vacating the premises. In the case of *Davis v. Moss* (1861), 38 Pa. 346, it was held that engines and pumps erected in a mine by a tenant did not become part of the real estate, but remained the tenant's personal property. In the case of *Heffner v. Lewis* (1873), 73 Pa. 302, a similar decision was made regarding iron rails laid by tenants in a tunnel. These rails were fastened to a track, but the court held that they might be sold under sheriff's proceedings against the tenants as their personal property.

In the case of *Albert v. Uhrich* (1897), 180 Pa. 283, it was held that the manner in which the fixtures are fastened to the real estate is not the best test as to whether they are legally removable. The true criterion is the intention which the tenant had when he placed the fixtures upon the property as to removing them during his term. Albert, the plaintiff in this case, had been running a mill on his wife's land, as her agent. He attached a boiler and engine to the milling plant. At that time the property was subject to a mortgage, and it was subsequently sold in proceedings for non-payment of the mortgage. After the sheriff's sale, Albert brought this suit to recover the boiler and engine. The court held that no intention to remove the fixtures could be presumed in such a case, for the wife had owned the premises when the boiler and engine were installed. Anyhow, the failure to remove them before the sheriff's sale debarred any subsequent attempt to do so. When fixtures are not removed before the tenant's

term expires, he loses his right to remove them. If, however, the lease is renewed, either by express or implied agreement, the tenant may remove fixtures erected during the original term while he remains in possession under the renewal contract.

Tenants of farming lands are entitled not only to crops which they sow and harvest during their term, but also to the *way-going crop*. In *Stultz v. Dickey* (1812), 5 Binney 285, this subject was discussed. An ancient Pennsylvania custom allows the tenant to return after the expiration of his lease and take away the crop of grain called the way-going crop, even though there is no clause in the lease giving him this right. This custom prevails, although the landlord has warned him not to sow the crop. The relation of landlord and tenant ceases with the expiration of the term and the surrender of possession, and the tenant is not bound to pay anything for the exercise of his privilege of removing the way-going crop.

Apparently, however, the tenant who has left the premises is not entitled to the way-going crop if he got the benefit of a winter crop at the beginning of the lease. *Comfort v. Duncan* (1836), 1 Miles 229. Moreover, this Pennsylvania custom is confined to fall grain, sown in the autumn before the lease expires, but cut in the summer after the tenant has removed. A tenant whose lease expires in April cannot sow grain in March with the expectation of getting it after it has ripened for harvest.

The tenant owes a certain loyalty to the landlord. While in possession under a lease, he cannot deny the landlord's title. The same rule governs a tenant holding over after his term expires. It would open the door to fraud if the claimant of land could gain possession by going in as tenant, and then assert ownership for himself. The landlord would be put at a disadvantage, for the tenant would be upon the premises, and might enjoy the use of them during the long stages of an ejectment suit. The tenant may, however, show that the landlord's title has come to an end. He is estopped from asserting that his landlord never possessed any title, but he may prove, for instance that the landlord has ceased to hold

it. The landlord may have sold his interest to the tenant himself or to a third party. Where a third party comes to the tenant and says that the property has been conveyed to him, the tenant should make sure of the truth of this assertion. If he pays rent to a strange party, who had no right to demand it, he must pay a second time to the rightful landlord.

PART IV

SALES OF REAL PROPERTY

CHAPTER XLVII.

CONTRACTS TO SELL REALTY AND CONVEYANCES THEREOF.

A contract to sell personal property is frequently executed at the same moment that it is first made by the seller's handing the article over to the purchaser. The delivery of possession in pursuance of the agreement transfers title at once to the purchaser. The transfer of real estate is a more formal matter. Usually there is, first, a contract providing for the sale, and, second, a conveyance in performance of the contract. This conveyance carries out the agreement of sale, and transfers legal title to the purchaser. The transfer generally takes place at the moment when the deed is delivered to the purchaser.

(A) The formation of a contract to sell realty.

In the seventh chapter we saw that the act of 1772 requires contracts for the sale of realty, or of any interests therein, to be in writing and signed by the seller or his agent. The agent's authority must be given in writing. There is little to be added here to what was said in the seventh chapter about the written memorandum of the contract. The agreement of sale should designate the realty in question with reasonable certainty. No technical words as, for instance, the word "heirs," need be used. On the other hand, a deed conveying a complete "fee-simple" title to the purchaser should contain the word "heirs." Thus, if you are selling a lot to John Smith, your deed should be made out to "John Smith, his heirs and assigns." The word "assigns" is usually employed, but is not necessary. The word "heirs" is necessary

in order to convey a complete title to John Smith, but is not necessary when the contract to sell the lot is formed.

When the owner of real estate agrees to sell it, certain steps must usually be taken before the conveyance can be properly put through. The first thing done in certain rare cases is to have the agreement of sale recorded in the county where the property is situated. This is occasionally resorted to in order to prevent an unreliable land-owner from defeating the agreement by selling to another party. A third person who makes settlement for property and records his deed is not affected by the fact that the seller had previously agreed to sell it to another, unless the third party actually knew this fact or unless there is some public record of the prior agreement which is legal notice to all the world. Options to purchase land are often recorded for a similar reason. In order that the contract of sale or the option may be put in proper shape for recording, it should be acknowledged before a notary. The form of acknowledgment should recite that the party agreeing to sell the land or giving an option to a prospective purchaser has acknowledged the agreement (or the option as the case may be) as his act and deed, and desired the same to be recorded as such. The use of the word "deed" in referring to an option or an agreement to sell land is technical. In popular use the word is restricted to mean a deed of conveyance. The legal definition of a deed, however, is as follows: "A writing containing a contract under seal, which is delivered by the party bound under the contract."

Assuming that the party who has agreed to buy land has decided whether or not to record the agreement, let us see what he should consider next. He should make sure that the seller's title is all right. If James Hill owns the property, it will do the purchaser no good to get a deed signed by William Jones. Assuming that the man who agreed to sell is really the owner, a further question arises as to whether there are liens against the property or anything else which should be removed. It takes some time to find out about these matters. Usually, therefore, an agreement of sale provides that it may be performed at any time within thirty days.

Where delay is expected, the parties sometimes allow a much longer time for performance. Frequently the purchaser may have difficulty in raising the money, and he should be careful to provide when the original agreement is signed for plenty of time within which to prepare himself to fulfil it. The following is a specimen form of agreement to sell real estate:

THIS AGREEMENT, made the third day of June, A. D. 1906, by and between William J. Mole, of the first part, and Philip Pack, of the second part, both of Philadelphia.

WITNESSETH, That the said William J. Mole hereby agrees to sell and convey to the said Philip Pack, who agrees to purchase the message or tenement and lot or piece of ground thereunto belonging, situate on the south side of Rittenhouse Street, west of Twenty-second Street, known as 2214 Rittenhouse Street, in the Eighth Ward, City of Philadelphia, for the sum or consideration of three thousand four hundred dollars (\$3,400) to be paid by the said Philip Pack in way and manner as follows, viz.: One hundred dollars to be paid at the time of signing this agreement and the balance at the time of settlement. A perpetual policy of fire insurance for \$2,000 is to be transferred to the party of the second part upon payment of the premium, less the discount named in policy, but is to remain with the mortgagee while the present mortgage is against the premises. The premises are to be conveyed free and clear of incumbrance and easements except an existing mortgage the amount of which is to be considered part of the purchase price above mentioned and except as to the lien of decedent's debts of the late Mary Mole. The gas fixtures, heaters, ranges, etc., annexed to the said building are included in the sale. Possession is to be given subject to tenant's monthly lease if tenanted at time of settlement. Taxes, water rent, interest on incumbrance and rent (if any) to be apportioned for the current term. Gas bills (if any) to be paid by the seller. The title to be such as will be insured by any first class title insurance company at regular rates. And the said parties hereby bind themselves, their heirs, executors and administrators, for the faithful performance of the above agreement within thirty days from the date hereof, time to be of the essence of this agreement unless extended by mutual consent in writing endorsed hereon. And the said Philip Pack hereby agrees to purchase the above described premises, from the said William J. Mole, for the price or sum above mentioned, and to pay and settle for the same, in the way and manner, and at the time above set forth. As Mary Mole, a former owner of this property, died within two years from the date hereof, the lien of her debts remains against it, but the purchaser assumes all expenses and trouble in connection with this matter and the taking of special title insurance against the same. The conditions of this agreement shall extend to the heirs, executors, administrators and assigns of both contracting parties.

IN WITNESS WHEREOF, the said parties to these presents have hereunto interchangeably set their hands and seals, the day and date first above written.

[Signed]	WILLIAM J. MOLE,	(Seal)
[Signed]	PHILIP PACK,	(Seal)

Witnesses present at signing,

[Signed] ADOLPH OBENLAND,

[Signed] WILLIAM A. MOONEY.

After the agreement has been signed, the purchaser should lose no time in having the title to the property searched. The custom throughout many parts of Pennsylvania puts the purchaser under the duty of having a deed of conveyance prepared, but this custom is not universal. The purchaser should usually arrange to get title insurance, which costs little and is a valuable protection. He should see that the company to which he applies for a title insurance policy is financially strong.

Within a week or two after the agreement of sale has been made, the conveyancer or title company that is making the searches for the purchaser should furnish him with a certificate showing how the property stands. This certificate will reveal whatever mortgages, ground-rents, judgments, mechanics' liens, municipal liens or other encumbrances are in the way of the seller's conveying a perfect title. It should inform the purchaser also of various other defects in the seller's ownership. Suppose, for instance, the seller has agreed to convey an entire city block to the purchaser. The title company should not only examine the records in the office of the Recorder of Deeds, but should also send an inspector to look at the land itself. If he finds that a lane runs through the property, and that it has been used for generations by the public, he will report this fact, and it will be noted in the certificate. The constant use of a lane by the public for over twenty-one years ordinarily deprives the owner of his right to resume exclusive possession of it. The prospective purchaser of the ground should be informed of the situation.

When a purchaser receives the settlement certificate, he should at once notify the seller about any liens or defects in the title mentioned by the certificate. Usually most of these can

be cleared off before the final settlement takes place between the parties. The purchaser should insist upon the seller's attending to them promptly. If they are not removed, the title company will note them as exceptions on its policy.

Sometimes, while preparations for a conveyance are being made, it is discovered that *the seller's wife refuses to sign the deed*. Her signature is highly important, for if she should not sign, the land would remain subject to her interest in it. A husband may validly mortgage his realty without his wife's consent, but he cannot sell it so as to defeat or impair her rights. In the fifth book we shall see what interest a wife has in her husband's estate. The wife's rights in her husband's realty do not mature unless she survives him. The purchaser, therefore, who learns that the seller's wife will not sign the deed, has the choice between refusing to go ahead with the transaction, on the one hand, and accepting a deed signed by the husband alone, on the other hand. In the latter case, he must pay the full purchase money. If he adopts the former course, he may recover damages from the husband for the expense to which he has been put. If he can show that the property was to have been sold for \$2,000, and was worth \$3,000, he cannot recover \$1,000 from the husband. To do this would probably result in forcing the wife to sign the deed against her will, which the courts would not sanction. The seller, however, may be compelled to pay the costs of conveying which the purchaser has incurred before learning that the seller's wife would not sign. If it appears that the husband has fraudulently persuaded his wife to withhold her consent, in order to back out of his agreement, he will be compelled to pay full damages for the breach of contract. In the case mentioned above where a \$3,000 property was agreed to be sold for \$2,000, the husband would have to pay \$1,000 to the disappointed purchaser if he had himself prompted his wife's refusal to join in the deed. It is sometimes wise to get the seller's wife to sign the original agreement of sale, in order to forestall possible trouble. *Huffman v. Bradshaw* (1901), 17 Super. 205.

Not every objection that may be raised by a title company will justify the purchaser in refusing to go ahead with

the contract. Usually the title companies act reasonably, and are willing to insure a title which is really good. If, however, such a company is over-critical, the purchaser will not usually be allowed to refuse to pay the price agreed upon, merely because he cannot obtain title insurance. The courts may uphold the seller's title, although title companies doubt its validity. Hence, in many agreements to sell realty a clause is inserted providing that the title must be such as will be insured by any reputable company engaged in that line of business. Sometimes the agreement mentions some particular company or companies upon whose decision the question of title is made to depend.

Suppose that the seller has acquired title merely by occupying the premises in defiance of the real owner for twenty-one years. Usually the real owner's rights are lost by his failure to assert them during that length of time. The holder of a title acquired in such a manner may compel a purchaser to accept it, if he can prove thoroughly that the former owner's rights are gone forever.

It is usually incumbent on the purchaser to see that the time allowed for the performance of the contract does not expire. If the seller's title causes a delay, beyond the time fixed for settlement, then he is the one to blame. If the time clause states specifically that time is of the essence of the contract, and one of the parties causes a delay beyond the limit fixed, the other usually has the privilege of dropping the matter, if he so chooses. It is usually provided that if the buyer fails to complete the purchase, the seller may retain the money paid on account as liquidated damages. In the case of *Clark v. Price* (1902), 19 Super. 582, Clark sued to recover money paid on account of the purchase price of land. The agreement of sale provided that Clark was to pay Price \$1,500 in all: \$275 cash upon the signing of the agreement, and the balance to be paid in monthly instalments of \$30 each, on the first day of each month. A certain allowance was made in Clark's favor, but it need not be mentioned here. It was further agreed that if Clark should default in the payment of any instalment for the space of six months, Price would have the

right at his option to rescind the sale, retaining the first six months' instalments as liquidated damages for the breach of contract, and returning the remaining instalments to Clark. Clark paid \$275 when the agreement was entered into, and thereafter one instalment of \$30 and one of \$25, making \$330 in all. Then he defaulted, but claimed that he was entitled to a return of \$275. The court held that the cash payment of \$275 was an "instalment" of the \$1,500 purchase money agreed to be paid. It was not a regular monthly instalment, as provided for in the agreement, but the stipulation did not mention the retaining of "monthly" instalments, but rather "the first six months' instalments." An instalment is a part of a debt due by a contract. It was not finally decided that Price should be allowed to retain the sum of \$330, but the court's opinion favored his contention.

(B) The performance of a contract to sell realty by delivery of the deed.

Assuming that the purchaser is satisfied with the title which the seller will convey, let us see what takes place at the actual settlement. If the deed has not already been executed, the seller (together with his wife if he is married) should be present. If he has authorized an agent to sign the deed for him, the power of attorney should be in writing, signed, sealed and acknowledged with the same formality as a deed of conveyance itself. The necessity for having it sealed and acknowledged is due to the fact that it will not otherwise be admitted to record. It should be in proper shape for recording, in order that the records may properly show the purchaser's chain of title, for a deed signed by an agent should not be accepted, unless it is accompanied by formal proof of authority. Usually, however, a seller of land who cannot personally attend the settlement does not go to the trouble of executing such a power of attorney. Instead, he has the deed sent to him in advance of the settlement, and, after executing it, returns it to his representative in the matter. The deed does not take effect at the time it is signed, sealed and acknowledged. It operates to transfer title only when it is delivered to the grantee. The

word "grantee" has a wider meaning than the word "purchaser," so far as concerns real estate. A grantee is one to whom a grant is made, and the name is applied to any party to whom property is conveyed by deed. The party who makes the conveyance is called the "grantor." Sometimes a deed is handed to a friend of both parties to a contract of sale, under an agreement that he shall deliver it to the grantee upon the happening of certain conditions. The title does not pass to the grantee until the friend who acts as an intermediary delivers it over to him. Where the deed is handed upon such a condition, not to an agent of the grantor, but to such an intermediary, it is called an escrow.

There is no particular necessity for the purchaser's attending a real estate settlement, provided that he has a capable representative. It is often desirable, however, for him as well as the seller to be present, for some unexpected questions may arise and call for an immediate decision. A careful lawyer or real estate agent may decline to decide such matters, unless he has been given general authority. The purchaser should see that sufficient cash is in readiness to pay whatever may be due by him at the settlement. He should provide an additional sum of money to cover such incidental charges as he may have to meet. Settlements are usually conducted on a strictly cash basis, and the purchaser should not embarrass himself by providing insufficient funds. He should not expect that the seller or title company will receive his check in payment unless this has been consented to beforehand. The certified check of a local bank or trust company is almost always accepted instead of cash.

It is preferable, where convenient, to have settlement take place at the office of the title company which is insuring the title. This facilitates the prompt adjustment of all open questions before the transaction is completed. You should, if possible, leave nothing for future determination when you are making settlement. If you disregard this rule, and permit the deed or the mortgage in question to be recorded, you may find that you have placed yourself in an awkward position. The contract has been largely performed by the recording of the document. It may become so difficult to undo what has been

done that you will have to sacrifice advantages which would have been gained by your insisting upon having everything straightened out before the settlement was completed.

The following forms of account show a settlement made through a title insurance company in pursuance of the agreement of sale set forth earlier in this chapter. The first account is the main one, as between the seller and the purchaser themselves:

No. 16,646.

PHILADELPHIA, PA., June 30, 1906.

SETTLEMENT between William J. Mole, seller, and Philip Pack, purchaser, for premises situate at 2214 Rittenhouse Street. Settled as of June 30, 1906.

PURCHASER, DR.

To purchase money, subject to \$2,200 mortgage.....	\$1,200.00	
" Fire Ins., No. 74,284, Girard Ins. Co., \$2,000, prem. \$40, less 10 per cent	36.00	
" Proportion of current water rent; whole rent \$...		
" Proportion of current taxes; whole tax \$45, 6 months	22.50	
" Rent of premises, from		
" Acknowledgment	50	
		\$1,259.00

PURCHASER, CR.

By cash paid on account	\$100.00	
" Proportion of current water rent; whole rent \$8, 6 months	4.00	
" Penalty thereon, 5 per cent	40	
" Proportion of current taxes; whole tax \$.....		
" Penalty thereon		
" Mortgage, \$2,200 as above		
" Interest on same from 6-15-'06 to 6-30-'06, 15 days at 6 per cent	5.50	
" Ground rent		
" Accrued rent thereon fromat %		
" Rent of premises from 6-30-'06 to 7-15-'06, half month at \$30	15.00	
		124.90
Balance due seller		\$1,134.10

[Signed]

WILLIAM J. MOLE, Seller.

[Signed]

PHILIP PACK, Purchaser.

It will be noted that the purchaser pays for the acknowledgment of the deed to him. He pays also for a proportionate part of the taxes assessed for the year 1906. As the settlement takes place on the last day of June, the year's taxes are borne equally by both parties. If the seller had not paid the taxes for 1906, instead of debiting the purchaser with half of them, the purchaser would be credited with half of them. He would take the premises subject to the lien of the 1906 taxes, and the title insurance policy issued to him would note that they were not paid, as an exception to a perfect title. Half a month's rent has been paid to the seller in advance by the tenant to whom the premises have been leased, and, therefore, the purchaser is credited with \$15. The water rent for 1906 has not been paid, and the purchaser is credited with half the yearly water rent, plus the entire penalty which the seller's failure to pay the water rent earlier in the year has caused the City Water Department to add to the usual payment.

The second account in the same transaction is as between the seller and the title insurance company. Suppose that there are two judgments which have appeared on the settlement certificate as defects in the title. Perhaps the seller has not had time or money to clear these off before the day of settlement, but he instructs the title company which handles the money paid by the purchaser to retain sufficient of this fund to pay off the judgments. The title company has carefully ascertained the exact amount due on these encumbrances. If this amount is less than what would be coming to the seller out of the settlement, the company will let the transaction proceed and hold back the amount, assuring the purchaser that the money will be applied to clear up his title. The following form of account shows the settlement of the title company with the seller :

Sales of Real Property.

SETTLEMENT WITH SELLER.

	Dr.	Cr.
By amount due from purchaser, as per statement.....		\$1,134.10
To taxes for the year		
" Water rent for the year		
" Mortgage		
" Interest thereon fromat %		
" Satisfaction		
" Principal of		
" Interest thereon fromat %		
" Judgments or claims, C. P. 5 D. 1905, No. 672,		
Judg't	\$540.10	
" " " " " 2 M. 1906, No. 410,		
Judg't	105.00	
" Recording		
" Notary Fees		
" Special Insurance, vs.		
		\$645.10
Balance due from the Equitable Trust Company to seller		\$489.00

Settlement and payments as above were agreed to and approved.

[Signed] WILLIAM J. MOLE, Seller.

The next account is as between the title company and the purchaser. This is the last part of the settlement. The purchaser must usually pay the company's charges, and these are, as a rule, paid at the time of settlement. Regular customers of title companies often prefer to have a bill rendered afterwards, paying at the settlement only what is due the seller. This plan is more convenient so far as recording charges are concerned, for it is sometimes hard to determine exactly what these will be. Usually the purchaser pays the estimated recording fees at the time of settlement, and, if the estimate proves incorrect, the matter is afterwards adjusted. Sometimes the purchaser's real estate agent will get the title company to include his fee for conveyancing or other services in their settlement with the purchaser. This course is adopted where the agent does not want to make out a separate bill, or is unwilling to wait for his money.

In the account given below it will be noted that the purchaser is charged for special insurance against the lien of

decedent's debts. William J. Mole is the owner of the property to be conveyed to Philip Pack. His wife, Mary Mole, was the previous owner, and left it to him by will. The act of June 8, 1893, fixes the time during which the debts of a decedent shall remain a lien on his realty at two years. Since the conveyance is made within two years of Mrs. Mole's death, the possibility that all of her debts may not have been paid is a cloud upon the title. Most purchasers, however, are willing to waive this defect, provided that the seller can induce the title company to insure against it. If the title company should find, for instance, that Mrs. Mole's estate is insolvent, they would refuse to insure against the lien of her debts. The best way to clear the title in that case would be for Mrs. Mole's executor or administrator to petition the Orphans' Court, and obtain permission for a judicial sale of the property. The purchaser at such a sale would buy clear of decedent's debts, and the money paid by him would be distributed among the creditors in accordance with law. Let us, assume in the case before us that Mrs. Mole's debts are believed to be fully paid. Nevertheless, the bare possibility that some unheard of creditor may turn up and assert his lien within two years is sufficient to necessitate special insurance against the decedent's debts. Ordinarily, William J. Mole, the seller, would have to pay for this special insurance, but the original agreement of sale provided that Pack should pay it, and it is charged to him in the account between the title company and the purchaser. It will be noted in the following account that Philip Pack does not advance the entire purchase money, \$1,200. He has borrowed \$800 from the Merrimac Building Association, which has deposited this sum with the title company to enable the settlement to go through. Pack has arranged to give the association a second mortgage on the property purchased by him, and this mortgage will be recorded by the company along with Pack's deed:

SETTLEMENT WITH PURCHASER.

Dr.		
To purchase money, as per statement.....		\$1,134.10
" Company's charges: Title Insurance, Premium and		
Examination Fee	\$26.00	
" Special Insurance vs. decedent's debts	12.00	
" Conveyancing	10.00	
" Recording	3.65	
" Notary fees		
" Transfer of Fire Ins. Policy.	50	
" Taxes for the year		
" Water rent for the year 1906	8.40	
" Amount due by purchaser to Company		60.55
" Total amount due by purchaser		\$1,194.65
Cr.		
By Amount deposited by purchaser with Company..		
" Amount deposited by Merrimac Building Association second mortgagee	\$800.00	800.00
Balance due by purchaser		\$394.65

Settlement and charges as above were agreed to and approved.

[Signed] PHILIP PACK, Purchaser.

The title company usually takes charge of recording all papers which are to be placed on record, and of transferring insurance policies. Delays in these matters are dangerous. If the buildings which are insured burn down before the transfer, the insurance company may refuse to recognize the policy which still stands in the former owner's name. If the deed is not promptly recorded, perhaps the rights of third parties may intervene, and defeat those of the negligent purchaser.

(C) The necessity of recording.

The act of May 19, 1893, directs that all deeds and conveyances made and executed within this Commonwealth concerning lands, tenements or hereditaments in Pennsylvania shall be acknowledged by the grantor or grantors before any of the judges of the Supreme Court, or before one of the judges of the Court of Common Pleas, or Recorder of Deeds, Pro-

thonotary, or clerk of any court of record, or justice of the peace, or notary public of the county wherein the lands lie, and shall be recorded in the office for recording deeds of the proper county within ninety days after the execution of any such deed or conveyance. Any deed or conveyance not recorded as aforesaid shall be considered fraudulent and void against any subsequent purchaser or mortgagee for a valuable consideration, or any creditor of the grantor. The act of 1893 allows six months for the recording of deeds and conveyances made and executed outside of Pennsylvania. The act of May 25, 1878, makes a special provision concerning the recording of deeds in cities of the first class. At present this act applies only to Philadelphia. It directs that deeds and conveyances of realty in such cities shall be recorded as soon as executed. Every such deed or conveyance shall be deemed fraudulent and void against any subsequent *bona fide* purchaser or mortgagee, unless such deed, conveyance or instrument of writing shall be recorded before the recording of the deed or conveyance under which such subsequent purchaser or mortgagee shall claim.

The object of these recording acts is to enable purchasers and mortgagees to assure themselves from the public records that the title offered to them is really in the party who claims to hold it, and is not subject to encumbrances. Almost everybody understands the necessity of promptly recording deeds and mortgages, and the recording acts rarely work injury to honest men who have been reasonably careful. On the other hand, the acts result in promoting the greatest confidence and certainty in real estate titles, which would otherwise cause endless confusion.

The recording acts do not affect the validity of a deed or mortgage as between the immediate parties. If a purchaser neglects to record his deed, that is no good reason why the seller should be at liberty to repudiate the transaction. Even third persons cannot take advantage of the failure to record if they have not been deceived. Suppose that A conveys his farm in 1905 to B, who fails to record the deed. In 1906 A fraudulently represents to C that he owns the farm, and C accepts A's deed. If C, before paying A for the farm, had

learned of the previous unrecorded conveyance to B, C could not shield himself behind the recording act. *The proper recording of a duly acknowledged deed constitutes legal notice to the world of its existence.* All are bound to heed this notice even without actual knowledge of the deed. C, having had *actual knowledge* of B's deed, cannot complain that he was not given record notice of it. Even if C was merely informed of facts which should have put him on his guard, and led him to inquire as to B's rights, he is not in the position of an innocent purchaser for value. A man cannot blindly trust to the appearances of public records, if he gets such notice that the records are incomplete as would make an ordinary reasonable man inquire further into the matter and learn the whole truth.

If a purchaser neglects to record his deed, only subsequent purchasers or mortgagees *for value* are protected by the recording acts. Suppose the seller afterwards fraudulently deeds the property over again to a relative, out of affection for the latter. The relative has no standing to complain of the purchaser's failure to record, because the second deed was not made to him for a valuable consideration. Again, if the seller dies, leaving his property by will to a friend, the latter has no right as against the purchaser. Again, if a judgment is obtained against the seller, the judgment creditor is not considered a purchaser for value. This would seem to be in conflict with the act of May 19, 1893, which directs that a deed not recorded for a certain period shall be considered fraudulent and void as against creditors of the grantor. The case of *Davey v. Ruffell* (1894), 162 Pa. 443, decided that this provision of the act of 1893 was ineffective, because there is no method by which a judgment creditor can put his judgment on record in the office of the Recorder of Deeds. A judgment appears in the records of the Prothonotary's office only.

In order to make the recording complete, so that a deed or mortgage may be legal notice to all the world, it should not only be copied into the Recorder's books, but also *indexed* in the alphabetical index which the Recorder keeps. The act of May 2, 1899, directs that all conveyances of real estate in counties of a population exceeding 500,000 shall be registered

in the office of the County Commissioners before being recorded in the office of the Recorder of Deeds.

The act of March 28, 1820, provides that all mortgages, or defeasible deeds of the nature of mortgages, should be promptly recorded. The Recorder must indorse on the mortgage or defeasible deed the time when it is left for record. If two or more are left on the same day, they shall have priority according to the time they were respectively deposited at the Recorder's office. Such mortgage, or defeasible deed in the nature of a mortgage is not a lien until it is left for record. The act of 1820 directs that a purchase money mortgage shall not be affected by these provisions, provided it is left for record within sixty days from its execution. A *judgment creditor has priority over the holder of an unrecorded mortgage*, except in the case of a purchase money mortgage recorded within sixty days of its execution. A distinction must, therefore, be drawn between the effect of the failure to record a deed and the failure to record a mortgage. As we saw in the case of *Davey v. Ruffell*, cited above, a judgment creditor is not within the protection of the acts for recording deeds. The reason for making this distinction is because the act of 1820 provides that no mortgage or defeasible deed shall be a lien until recorded or left for record.

The act of June 4, 1901, P. L. 425, directs that when a resulting trust as to real estate arises through the payment of the purchase money by one person and the putting of legal title in another's name, such a trust shall have no effect as against *bona fide* judgment creditors or other creditors or mortgagees of the holder of the legal title or purchasers from such holder without notice of the trust, unless either (1) a declaration of trust has been executed and acknowledged by the holder of the legal title, and recorded in the Recorder's office of the county where the land is situated, or (2) unless an action of ejectment has been begun in the proper county by the person advancing the money against the holder of the legal title. Something is said about implied trusts on page 126.

CHAPTER XLVIII.

RIGHTS AND OBLIGATIONS OF THE PARTIES TO A SALE OF REAL ESTATE AFTER THE TITLE HAS PASSED.

We shall assume that a settlement has been made, and that the purchaser's deed has been recorded. Usually this is the final step in the performance of the contract of sale. The parties ordinarily have no further legal relation with each other as respects the contract, which has been discharged by performance. In many cases, however, the recording of the deed does not terminate the relation between the seller and purchaser. Perhaps the purchaser has not paid the entire price in cash, and has given the seller a mortgage for the balance of the purchase money upon the premises in question. Perhaps the seller has given the purchaser a warranty that the title is absolutely clear, but it comes to light afterwards that it was subject to an old encumbrance. In either case, the parties will have further dealings with each other, and the relationship established by the former transaction is of legal importance as affecting these dealings.

The subject matter of this chapter may be treated under two heads: first, the obligations of the seller towards the purchaser; second, the obligations of the purchaser towards the seller.

(A) The obligations of the seller towards the purchaser.

It was stated in the preceding chapter that the purchaser of realty should ascertain the condition of the title beforehand, and have it cleared of all defects before the settlement. Sometimes this rule is not followed, because the purchaser neglects to have the title properly searched. Sometimes again, he learns of defects in the title, or encumbrances on the real estate, but agrees to buy subject to them.

Where the title received by the purchaser is not as good as he had expected, his rights against the seller depend in a large measure upon the deed which the latter signed. If it was

merely a *quit-claim deed*, the disappointed purchaser seldom has any right of action against the seller. The following is a specimen of such a deed:

"Know all men by these presents, that I, Howard Gay, of the Borough of Bristol, in the County of Bucks and State of Pennsylvania, for and in consideration of the sum of \$500, to me in hand paid, [or secured to be paid], by Mary Menz, of the said borough, the receipt whereof is hereby acknowledged, have remised, released and quit-claimed, and by these presents do remise, release and quit-claim unto the said Mary Menz, and her heirs and assigns, forever, all that, etc. [here describe the premises]: together with all and singular the tenements, hereditaments and appurtenances thereunto belonging or in any wise appertaining, and the reversions, remainders, rents, issues, and profits thereof; and all the estate, right, title, interest, claim or demand whatsoever of me, the said Howard Gay, either in law or equity, of, in, and to the above bargained premises, to have and to hold the same to the said Mary Menz, and to her heirs and assigns forever.

"In witness whereof, etc."

This deed should be acknowledged and recorded in the same manner as the ordinary deed of conveyance. The words, "tenements, hereditaments and appurtenances" appear in many documents relating to real estate. The word "tenements" refers to realty, and it is employed because it has a more extensive meaning than the word "lands." It was used in ancient times to transfer title to various feudal rights which were connected in England with the ownership of lands. The word "hereditaments" had an even wider significance than the word "tenements," covering everything capable of being inherited as real estate. It included heirlooms and certain furniture which in England often passed with the land when it descended upon the owner's death to his heirs. The word "appurtenances" also refers to incidental rights connected with the ownership of lands, as, for instance, a right of way to walk across certain neighboring land in order to reach a spring.

Suppose that instead of a quit-claim deed, as exemplified in the foregoing form, Howard Gay had signed a deed reciting

that he did thereby "*grant, bargain and sell*" the premises described to Mary Menz. The act of May 28, 1715, provides that the use of these words in a deed conveying real estate in fee simple shall be equivalent to an express agreement with the grantee, and his heirs and assigns as follows: That the grantee owned an indefeasible estate in fee simple, free of encumbrances done or suffered by the grantor, as also for quiet enjoyment of the premises against the grantor, his heirs and assigns, unless limited by express words contained in such deeds. The use of these words, therefore, implies an agreement that, while the seller has been the owner of the property, he has *done or suffered* nothing to impair the title. Thus, if he had mortgaged the premises and afterwards sold them by a deed which contained the words "grant, bargain and sell" without any reference to the mortgage, he would commit a breach, for which the purchaser could hold him liable. The words in question would imply that the seller had not placed any encumbrances upon the premises. If the seller has had judgment entered against him in the county where the lands lie, this judgment is a lien against the lands if owned by him when judgment was obtained. The lien lasts for five years, but should be renewed every five years so that it may still bind the realty. When renewed, it binds realty acquired after judgment is obtained. Suppose that such a judgment is a lien upon the premises at the time of the sale. The seller has "*suffered*" the recovery of judgment against him. If the words "grant, bargain and sell" are used in the deed without mention of the judgment, the purchaser may sue the seller for his breach of contract. See as to liens *Brown's Appeal* (1879), 91 Pa. 485.

The technical words which we have been considering do not imply an agreement that the title is absolutely perfect. If there are encumbrances and defects antedating the time when the seller first acquired ownership, he cannot be held responsible for them, merely because these words appear in the deed. We have seen that usually in the ordinary sale of personalty there is an implied warranty of an absolutely clear title. The rule is different in the case of real estate sales, and, therefore, the purchaser should try to have a general warranty clause

inserted in the deed. His main reliance may be placed upon the title insurance policy which he should ordinarily obtain, but it is wise to get also an agreement from the seller governing this matter.

We have seen that a purchaser may refuse to pay down his money at the settlement, if the seller cannot convey a good title. If the purchaser fails to learn of defects in the title until after he has paid the purchase money, he is unable to recover his money unless he proves a breach of contract. Suppose that there has been no agreement to convey a clear title, and that the discovery of defects in it is made after the settlement but before the securities given for the purchase price have been fully paid. Is the purchaser justified in refusing to pay the notes or mortgage bonds or other instruments which he has given to secure the purchase price? Except in the case of a mere quit-claim deed the rule is that the purchaser may prevent the enforcement of his promise to pay the purchase money by showing that the title is defective. Where, however, the purchaser's only complaint is that the land conveyed was somewhat smaller in extent than would appear from the deed, he cannot after settlement refuse to pay the notes or bonds given to secure the purchase money, unless a survey of the premises was made before the settlement. If the deficiency in the amount of real estate was very great, so that the usefulness of the purchase is destroyed, the rule is different. In any case, however, where the deed clearly shows that the purchaser took the risk of defects in title or of any misdescription, he cannot successfully defend a suit for the purchase money.

The following deed is drawn up according to a form sanctioned by long usage. It contains a general warranty clause, about which something will be said later :

THIS INDENTURE, made the thirtieth day of June, in the year of our Lord one thousand nine hundred and six (1906), between William J. Mole, of the city of Philadelphia, sole devisee under the will of Mary Mole, late of the City of Philadelphia, deceased, of the one part, and Philip Pack, of the city aforesaid, of the other part.

WITNESSETH, That the said William J. Mole for and in consideration of the sum of twelve hundred dollars (\$1,200.00), lawful money

of the United States of America, unto him well and truly paid by the said Philip Pack, at and before the sealing and delivery of these presents, the receipt whereof is hereby acknowledged, *hath* granted, bargained, sold, aliened, enfeoffed, released and confirmed, and by these presents *doth* grant, bargain, sell, alien, enfeoff, release and confirm unto the said Philip Pack, his heirs and assigns.

All that certain three-story brick messuage or tenement (No. 2214) and lot or piece of ground *situate* on the south side of Rittenhouse (formerly F) Street, at the distance of one hundred and thirty-three feet westward from the west side of Twenty-second Street, in the Eighth Ward, of the City of Philadelphia aforesaid.

Containing in front or breadth on the said Rittenhouse Street sixteen feet and extending in length or depth of that width southward sixty-two feet to Manning Street. *Bounded* eastward by ground now or late of John Sailer; southward by said Manning Street; westward by premises of Emma M. Smith and northward by Rittenhouse Street aforesaid. Being the same premises which Matilda Acker by indenture dated the ninth day of September, A. D. 1898, and recorded in deed book W. M. G. No. 346, page 128, etc., granted and conveyed unto the said Mary Mole in fee. *Under and subject* to the payment of a certain yearly ground rent of fifty-four dollars, which said ground rent Joseph Ward, by indenture bearing date April 11, A. D. 1906, and recorded in deed book W. S. V. No. 646, page 124, assigned unto the said William J. Mole, whereupon the said ground rent ceased, merged and became forever extinguished.

Under and subject to a certain mortgage debt or principal sum of twenty-two hundred dollars (\$2,200.00) with interest secured thereon as and when it becomes payable. And the said Mary Mole, being so thereof seized, departed this life on or about the sixth day of October, A. D. 1904, having first made and published her last will and testament in writing bearing date the thirtieth day of September, A. D. 1904, duly proved October eleventh, 1904, and registered in the office of the Register of Wills in and for the City of Philadelphia in Will Book No. 262, page 16, etc., wherein and whereby she did provide as follows, to wit: "I give, devise and bequeath to my husband, William J. Mole, all my real, personal and mixed estate of whatsoever nature or kind and wherever situate, after the payment of my debts and funeral expenses, absolutely."

Together with all and singular the buildings, improvements, streets, alleys, passages, ways, waters, water courses, rights, liberties, privileges, hereditaments and appurtenances whatsoever thereunto belonging or in anywise appertaining and the reversions and remainders, rents, issues and profits thereof, and all the estate, right, title, interest, property, claim and demand whatsoever, of him the said William J. Mole, or otherwise howsoever of, in and to the same and every part thereof.

To have and to hold the said three-story brick messuage or tenement and lot or piece of ground hereinbefore described, hereditaments and

premises hereby granted or mentioned and intended so to be with the appurtenances unto the said Philip Pack, his heirs and assigns, to and for the only proper use and behoof of the said Philip Pack, his heirs and assigns forever *under and subject*, nevertheless, to the payment of the aforesaid mortgage debt of twenty-two hundred dollars (\$2,200.00) with interest.

And the said William J. Mole for himself, his heirs, executors and administrators, doth by these presents covenant, grant and agree to and with the said Philip Pack that he, the said William J. Mole, his heirs, executors and administrators, the above described messuage or tenement, and lot or piece of land, hereditaments and premises hereby granted, or mentioned or intended so to be, with the appurtenances, unto the said Philip Pack, his heirs and assigns, against him, the said William J. Mole and his heirs and against all and every person or persons whomsoever lawfully claiming or to claim the same or any part thereof, shall and will, subject as aforesaid, warrant and forever defend.

IN WITNESS WHEREOF the said William J. Mole has hereunto set his hand and seal the date and year above written.

[Signed] WILLIAM J. MOLE. (Seal)

Sealed and delivered in
presence of us.

[Signed] N. A. KRONING,

[Signed] JOHN J. WILLIAMS.

On the thirtieth day of June, A. D. 1906, before me, the subscriber, a Notary Public of the Commonwealth of Pennsylvania for the City and County of Philadelphia, personally appeared the above named, William J. Mole, and in due form of law acknowledged the above indenture to be his act and deed, and desired that the same might be recorded as such.

Witness my hand and notarial seal the day and year aforesaid.

[Signed] N. A. KRONING,

Notary Public.

(Notarial Seal.)

Commission expires February 9, 1907.

The foregoing form of deed contains a general warranty clause, because Mole covenants, promises and agrees to and with Pack, the grantee, for the benefit of Pack and his heirs and assigns that he will forever warrant and defend the title against *every person or persons whomsoever*, lawfully claiming or to claim the same or any part thereof. This general warranty clause could have been converted into a special warranty clause by inserting after the word "thereof" the following words "by, from or under him, them, or any of them." These last words

if inserted would have virtually limited Mole's obligation to defend the title to cases in which proceedings might be brought upon claims arising during Mole's ownership of the premises. The general warranty clause extends farther back. If, for instance, loss should be caused to the purchaser, Philip Pack, by a defect in the title dating back more than a century, he would be justified, under the general warranty clause, in calling upon Mole to indemnify him.

(B) The obligations of the purchaser towards the seller.

The main object which the seller of land has in view is almost always that of obtaining money for it. If the purchaser pays what he has agreed, the seller has seldom any further demand upon him. Trouble is sometimes caused, however, where the purchaser agrees to buy property *under and subject* to an existing mortgage, ground-rent or other encumbrance. The act of June 12, 1878, provides that a grantee of real estate which is subject to a ground-rent, mortgage or other encumbrance shall not be personally liable for the payment of same, unless he shall, by a written agreement, have expressly assumed personal liability therefor, or unless there are express words in the deed of conveyance stating that the land is conveyed on condition that the grantee assumes such liability. The use of the words "under and subject to the payment of such ground-rent, mortgage or other encumbrance," shall not alone be so construed as to make the grantee personally liable. The right to enforce such personal liability where the grantee assumes it, does not inure to the benefit of any person except the one with whom it is made. Neither does the personal liability of the grantee continue after he has *bona fide* parted with the encumbered property, unless he shall have expressly assumed such continuing liability. See the case of *Schmidt v. Gibson* (1903), 12 D. R. 561.

Until the seller's deed is delivered, he retains a lien for his purchase money upon the real estate. This rule reminds one of the rule concerning the sale of personalty, namely, that the seller before delivering possession of the personalty usually retains a lien on it for the purchase money. The land cannot

be handed over to the purchaser in the same way as movable articles of personal property. The delivery of the deed, which represents the title and ownership, roughly corresponds to the manual delivery of tangible articles of personal property.

As soon as the deed has been delivered to the purchaser, the seller loses control of the property. Even though the purchase money has not been paid, he has no lien against it, unless he has obtained a mortgage upon it or some other encumbrance to secure payment of the price. In this respect he is like the owner of personalty who sells it on credit, and delivers possession to the buyer. The seller of real estate cannot retain a lien for the purchase money merely by remaining in possession. Where the purchase money is not paid he should have it secured to him either by a mortgage or a ground-rent upon the premises conveyed.

Where the buyer is not required to pay all of the purchase money at the time of settlement, he usually gives a mortgage to secure the balance. This mortgage should be recorded at the same time as the deed. Instead of taking a purchase money mortgage for unpaid purchase money, the seller sometimes reserves a ground-rent when conveying property. The advantage of a ground-rent is that it is not assessed for taxation, while the holder of a mortgage must pay a yearly state tax of four-tenths of one per cent. The disadvantage of most ground-rents is that the principal cannot be called in by the holder. The owner of property against which the ground-rent stands may pay it off after the period fixed by the parties, which must not exceed twenty-one years. Formerly irredeemable ground-rents could be created, but this is now forbidden by statute. The inability of the holder of a ground-rent to call in the principal is a dangerous feature of such securities, because the premises out of which the ground-rent issues may greatly decline in value. Recently some ground-rents have been made which contain a clause enabling the holder to demand the principal debt. Some sellers of real estate save the trouble of having a purchase money mortgage drawn up by taking a judgment note for the unpaid balance of the purchase money. The judgment note is entered up in the Prothonotary's office

in the county where the land lies, and creates a lien on the premises. The disadvantage of this form of security is that judgment liens are often lost without the lienholder's knowledge. A first mortgage is a safer security, for it can seldom be disturbed by sheriff's sale without the mortgagee's knowledge. Suppose, for instance, you have a first mortgage on certain property, and the owner makes a second mortgage. If he does not pay interest on the second mortgage, the second mortgagee may have it reduced to judgment, and sell the property at sheriff's sale. The sale will not, however, destroy the prior lien of your mortgage. If you had taken a judgment note and entered it up, instead of taking a mortgage, a sheriff's sale under a judgment note subsequently entered up or under a subsequent mortgage would destroy your lien as respects the property sold. If the proceeds of the sheriff's sale were sufficient to pay the amount of your judgment, you would probably lose nothing, because you would have a priority in the distribution of such proceeds over the holder of the subsequent judgment note or mortgage. If, however, the sheriff's sale did not realize sufficient to pay your judgment in full, you would have lost your lien on the realty without getting completely paid from its proceeds.

Another disadvantage of being a mere judgment creditor, instead of a mortgage creditor, is that you have no interest upon which to take out a policy of fire insurance on the judgment debtor's property; while a mortgage creditor has an insurable interest in the mortgaged property. See *Light v. Insurance Co.* (1895), 169 Pa. 310.

BOOK FOURTH

SURETYSHIP AND GUARANTY, AND INSURANCE

PART I

SURETYSHIP AND GUARANTY

CHAPTER XLIX.

THE NATURE AND FORMATION OF THE CONTRACT.

(A) Nature of the contract.

Contracts of suretyship or guaranty, and contracts of insurance are alike in that one party undertakes to compensate another for a loss contingent upon an event uncertain either as to its happening at all, or its time of happening; in suretyship or guaranty such loss is contingent upon the non-performance of a third party's obligation; in insurance the loss is contingent upon the destruction of the property of the insured, or the occurrence of his sickness or death, or, in fact, upon any injury to a specified subject by specified perils. We shall treat suretyship and guaranty in the first part, and insurance in the second part of this fourth book.

At the outset an original, independent undertaking must be carefully distinguished from a contract of suretyship or guaranty. A party who makes an original undertaking assumes sole liability for the performance of his part of the transaction; while a contract of suretyship or guaranty is an agreement to answer for the debt or default of another. The original under-

taking involves a primary liability; the contract of suretyship or guaranty involves only a secondary liability depending upon the default of *another* who is primarily liable.

Besides the importance of this distinction in determining just who is liable in the first instance, it is valuable for other reasons. Proof is simpler if suit is brought on an original undertaking. If suit is brought on a contract of suretyship, the plaintiff must show that the principal debtor has not paid. If the transaction was a guaranty, it must be shown either that the debtor is insolvent or that the plaintiff has used due diligence in pursuing him. There are defences which a surety can make that cannot be made by one who is bound in an original undertaking; for instance, extension of time to the debtor, without notice to the surety, which will be considered in Chapter LI.

The following cases illustrate how the courts distinguish an original undertaking from a contract of suretyship or guaranty. In the case of *Goodman v. Wireman* (1881), 2 York 175, it appeared that Wireman had signed the following order directed to Goodman: "Any goods you sell Gibson in amount not exceeding \$100 I will pay you in ninety days. I know Gibson to be reliable." The court treated this order as an original undertaking by Wireman to pay for \$100 worth of goods to be sold to Gibson, and said that there did not seem to be any idea in Wireman's mind that the goods were to be paid for by Gibson himself. That being so, Wireman was the principal debtor, and no question of suretyship or guaranty could arise. In *Watson v. Porzel* (1893), 158 Pa. 513, the defendant had given to Watson the following writing: "Send Miller six gross export beer bottles, and put down his order for fifty gross of full quarts." The court held that the undertaking was an original one to pay for the goods specified in the writing, and the defendant was primarily liable thereon, rather than Miller.

A contract of suretyship or guaranty is an agreement to answer for the default of another. A suretyship obligation is a direct liability assumed by a third person to the creditor for *the act* to be performed by the debtor, while a guaranty creates a liability only for the debtor's *ability to perform the act*.

The importance of the distinction is that in the former the undertaking is immediate and direct that the act shall be done, which, if the act is not done, makes the surety responsible at once; while in the latter, the guarantor undertakes that his principal, the debtor, is able to perform. Hence, a guarantor is not liable until the debtor is shown to be insolvent, or until the creditor shows that he has used due diligence against the debtor, while a surety is liable in the first instance. *Reigart v. White* (1866), 52 Pa. 438. A surety undertakes to pay if the debtor *does not*, while a guarantor undertakes to pay if the debtor *cannot*. The one is an insurer of the *debt*, the other an insurer of the *solvency* of the debtor. *Kramph v. Hatz* (1866), 52 Pa. 525. The leaning of the courts is against construing such contracts to be guaranty contracts, and against requiring the creditor to show diligence in pursuing the principal debtor on the latter's insolvency. *Woods v. Sherman* (1872), 71 Pa. 100; *Trust Co. v. Boyer* (1905), 15 D. R. 45.

(B) *Formation of the contract.*

1. *Formality and consideration.*—Under the act of 1855, as was shown in Chapter VII, a promise to answer for the debt or default of another must be in writing. It must also be remembered that verbal evidence is generally inadmissible to vary the terms of a written instrument. This emphasizes the importance of having such contracts written clearly, accurately and so as to contain the complete agreement of the parties. The necessity of having a contract of suretyship or guaranty written does not dispense with the requirement that it must have all the five elements noticed in the first book as essential to every valid contract. With respect to consideration, in *Conmey v. Macfarlane* (1881), 97 Pa. 361, it is said: "The consideration is the favor the surety receives from a compliance with his express or implied request that *credit* should be *given to the principal*." Or, again, where a debt has been already incurred, as in *Downing v. Funk* (1835), 5 Rawle 69, the *creditor's promise to wait* for his money at the request of the surety is consideration for the surety's undertaking to become responsible. Again in the case of *Nugent v. Wolfe* (1886),

III Pa. 471, the court stated that "the consideration for the promise of the principal is a *good consideration* for the promise of the surety or collateral promisor. *The credit is given as well upon the original consideration of the principal as the collateral promise of the surety, and is a good consideration for both.*" The last part of the foregoing quotation calls our attention to an application of Rule 2 on consideration, in Chapter III, namely, the principle that a single promise or consideration moving from one party may support and balance a double promise moving from the other party to the contract.

2. *Parties; agency; partnership; co-sureties.*—There are many cases in which a friend acts as surety, where a surety company would not feel justified in taking the risk. As a matter of business prudence it is much better to have a surety company act in such a matter, wherever possible, because a company knows best how to minimize the risk, and to safeguard the interests of the creditor. It should be much more satisfactory to a debtor to procure a surety company to go his security, than to ask a friend who may not feel that he can refuse. If a surety company acts in the matter, the transaction rests upon a strictly business basis; the creditor is well protected, and the debtor is not subjecting any of his friends to a risk of loss.

In connection with the subject of parties, notice *Talmage v. Burlingame* (1848), 9 Pa. 21, which decides that a contract of suretyship may be made without the knowledge of the debtor, and without his becoming a party thereto. The court said: "The absence of a request by the original debtor inducing the undertaking, does not absolve him (the surety) from it, for nothing is clearer than that a stranger may, for a consideration, bind himself to pay the debt of another without his privity or knowledge. * * * The contract of the surety is with the creditor and not with the debtor. * * * No doubt can exist that one may become a surety at the request of a creditor, provided a consideration passes."

The practical value of the foregoing decision to a business man is as follows: Often a merchant may have a chance to make a sale, and yet not consider it safe to do so without

security that he will be paid. He may not wish to risk losing the sale by demanding that the prospective purchaser furnish security. But he may secure himself without requiring the debtor to procure the surety. It is not uncommon for salesmen, who come directly in contact with customers personally unknown to the employer, to guarantee the payment of the price of the goods. Salesmen who work on a commission basis are often willing to do this in order to make a sale, and thereby earn their commissions.

A creditor, before accepting security from an agent who assumes to bind his principal as surety, should take care to see that the agent is duly authorized to make such a contract. See the case of *Stevenson v. Hoy* (1862), 43 Pa. 191, in which it appeared that an agent had entered into a contract of suretyship on behalf of his employer. The agent had authority to write letters in his employer's name, to collect money and give receipts therefor in the employer's name, and to indorse bank checks in the employer's name, which checks were always paid without question. The guaranty was given in the name of the principal for goods purchased by the agent. In a suit against the employer upon his alleged contract of guaranty, it was held that the plaintiff could not recover, because the defendant's agent had no authority to make the contract.

A creditor, in taking security from a member of a firm and expecting to obtain the firm obligation, must be sure that the partner with whom he deals is acting in the regular course of business in entering into the contract. In *Sutton v. Irvine* (1824), 12 S. & R. 13, the court said:

"The law is well settled, and it comports with all justice and reason that it should be so settled, that a guarantee by one partner in the partnership name, unless it is in the regular line of business, cannot bind the other partners; but if it be afterwards adopted and acted upon, it does bind them."

In order to have the surety bound at once upon the delivery of the contract it must be unconditional and absolute. If there is a condition known of by the party to whom the surety is to be bound, such as that certain others are to become co-sureties, a surety is not liable until the co-sureties are obtained. *Keener v. Crago* (1874), 81* Pa. 166.

One who executes a bond as surety may protect himself from being the only one liable thereon by an express stipulation that he shall not be liable until certain others shall have executed it with him. We learn from *Whitaker v. Richards* (1890), 134 Pa. 191, that, in the absence of some such stipulation, the bond, although it was prepared for the signatures of other persons who are named in it as sureties, but do not execute it, will bind all others who do execute and deliver it.

3. *Communication of acceptance.*—If a merchant declines to sell goods to another on credit, unless he is secured, and a third person writes to the seller that he will be responsible for payment if the goods are immediately delivered to the buyer, the third person is bound without a notice from the seller accepting his offer to become surety. See *Reigart v. White* (1866), 52 Pa. 438.

A guarantor of future credit is, however, entitled to notice from the party giving the credit, of his acceptance of the guaranty. *Kay v. Allen* (1848), 9 Pa. 320. In that case, it appeared that Kay had told a man named Martin that he would supply the latter with goods if Martin would procure a "satisfactory person to underwrite him." Then Allen wrote: "I would recommend Martin, and would go security for him to any reasonable amount; so you can fill this order and feel yourself as secure as when I was doing business with you." The goods were furnished on the strength of this letter. In a suit by Kay against Allen, it was held that the plaintiff could not recover, as notice to defendant of the acceptance of the guaranty had not been shown. See also *Gardner v. Lloyd* (1885), 110 Pa. 278.

It is held in *Coe v. Buchler* (1885), 110 Pa. 366, that one who offers to guarantee a contract which has not been signed or accepted by the parties, is entitled to notice of acceptance; and such notice will not be presumed from the fact that the guarantor must have been aware that goods were furnished after the guaranty had been signed.

The guarantor may be entitled to notice of acceptance, although the principal may not be entitled to express notice of the acceptance of his own offer. *Acme Manufacturing Co. v.*

Reed (1900), 197 Pa. 359. A blank form for ordering goods sent out by the Acme Company was filled up by a customer. A guaranty was endorsed on the order, and the order was returned to the corporation. The order contained a stipulation that the same would be considered as accepted by the corporation unless notice was given to the contrary within thirty days of the receipt of the order. The corporation accepted and filled the order, but gave no notice of the acceptance to the guarantor. The guarantor was not liable.

In all such transactions we should keep in mind the position of the parties in the making of the contract. If the party who is to go security is the offeror, the other party, the creditor, is the offeree, and must in some way show his acceptance of the offer in order to make a binding contract. However, if the offer to take another as surety or guarantor comes from the creditor, such other is the offeree and becomes bound the moment he accepts the offer to take his security. In such a case, the creditor is not bound to notify the offeree of the acceptance of the acceptance. See as to notice of acceptance *Radiator Co. v. Hoffman* (1904), 26 Super. 177.

4. *Reality of consent*.—When a man undertakes to go security, fairness is essential to the validity of his obligation. If he is deceived in any way, or treated fraudulently he may refuse to perform his agreement. In *Bots v. Stuhl* (1897), 4 Super. 52, the court said:

“When a contract of suretyship is entered into, the surety is entitled to know all the material facts concerning it, and if the person for whose benefit the suretyship is contracted conceals any material fact of importance in the determination of the surety to undertake the contract, such concealment is a fraud upon the surety and will vitiate the contract.”

Goebel Brewing Company v. McLean (1900), 15 Super. 38, is an interesting example of imposition upon a surety by concealing material facts from him. The brewing company entered into an agreement to sell and deliver beer to Nelson. After the parties had been dealing with each other for more than a month, Nelson gave a check to the brewing company to pay for a carload of beer. The check was protested and was

not paid. Later Nelson became further indebted to the company, the indebtedness reaching a total sum of \$1,100. The company refused to make further sales under the contract unless Nelson gave a bond. The brewing company's agent went to McLean and requested him to go Nelson's security. When the surety bond was shown to McLean he said that he disliked the idea of going security, but the company's agent said: "I assure you it is all right; Nelson has friends and can dispose of the quantity of beer I have stated." McLean then said that he understood that Nelson was just starting in business, and, there being no dissent from that proposition, he inquired of the agent whether that was all right. The agent replied: "I think so." McLean then executed the bond, the material facts in regard to Nelson's indebtedness to the company being concealed from him by the agent of the company and by Nelson. It was held that the surety was not liable because of the imposition upon him.

Meek v. Frantz (1895), 171 Pa. 632, is a clear illustration of such fraud as will relieve a surety from liability on his obligation. In that case a lease had been made, and after the lessee had signed the lease the lessor asked a third party to become surety on the lease, although this was contrary to the desire of the lessee. The third party was induced to sign as surety by the lessor's false representation that the lessee wished him to do so. The surety was not liable.

If there was no fraud, a surety or guarantor cannot avail himself of the fact that he did not read the contract when he signed it. A man is bound to read a contract before he signs it, unless he is willing to take the risk of obligating himself to do anything the instrument requires of him. *Johnston v. Patterson* (1886), 114 Pa. 398. One who is fraudulently induced to sign a contract without first reading it cannot, however, be held liable under it, except in some cases where the rights of innocent third persons are concerned.

CHAPTER L.

THE TERMINATION OF THE CONTRACT.

Much of what was said in Part IV of Book First under the heading "Discharge of Contracts" applies to the special class of contracts of suretyship and guaranty here being treated. In that place it was stated that contracts may be discharged in five ways: first, by agreement; second, by performance; third, by breach; fourth, by impossibility; and, fifth, by bankruptcy. These five means of discharging contracts will be used here as a basis for treating the discharge of the contracts we are now considering. When the word "surety" is used in this chapter it is usually to be taken for granted that what is said applies to guarantors also, unless the contrary appears from the context.

(A) Discharge by agreement.

As in ordinary contracts, the surety and the creditor may come to an express agreement that the surety is no longer to be held liable for the default of the debtor, but it must be remembered that the creditor's promise to release the surety must be under seal or supported by consideration. The agreement to discharge the surety is sometimes implied from the action of the creditor. For example, a creditor who releases his debtor clearly implies by such action a release of the surety. When the original debt is cancelled there can be no default of the debtor upon which the surety may be held liable. If the creditor even releases collateral or other property of the debtor upon which he might realize in satisfaction of his debt, the surety for such a debt is to be considered released from liability to the extent that such release has damaged him. *Hutchinson v. Woodwell* (1885), 107 Pa. 509.

Although granting an extension of time to the debtor, or releasing him in any way, often releases the surety, on the other hand, the creditor may safely grant an extension of time

to the surety or release him altogether, without affecting the principal's liability.

(B) Discharge by performance.

Naturally enough, the payment of the debt or performance of the undertaking by the debtor releases his surety. The surety's liability is conditioned on non-performance of the undertaking by the debtor; performance, then, releases the surety.

(C) Discharge by breach.

Any material change in the contract between the principal debtor and the creditor, made without the surety's knowledge and assent, will discharge him from liability.

A surety or guarantor who goes security is presumed to take into consideration the terms of the contract between the debtor and the creditor in deciding whether or not he should do so. It is plain that he may be willing to become liable where the debtor is undertaking to do certain stipulated things, although he might not agree to become liable if the debtor had stipulated to do other and different things. An illustration of this is the case of *Mercer County v. Coovert* (1843), 6 W. & S. 70, in which the defendants signed an agreement to guarantee the payment of \$1,300 to the Commissioners of Mercer County, to aid in the construction of a bridge at a particular spot, the plaintiff to pay the residue. The bridge was not built at the spot, but at another place less advantageous to some of the defendants. It was held that the defendants were not liable, because they had not offered to contribute to the expense of a bridge at any other place than at the spot specified.

In *Yohn v. Shumaker* (1897), 5 Super. 320, a judgment note had been signed by one as surety for another. The surety signed the note in blank. The creditor entered up judgment on the note. The surety applied to the court to have the judgment opened, alleging that the note was to be payable in six months, but that a dispute had arisen subsequently between the creditor and the principal debtor, and the

principal debtor had refused to sign the judgment note. At this stage of the transaction the creditor's attorney had filled out the note and made it payable "at once." The surety never consented to any such change in the judgment note. The court held that making the note payable at once, when it was to be made payable in six months, was a material alteration of the contract which rendered the note void. In *Nesbitt v. Turner* (1893), 155 Pa. 429, an action was brought against a surety on a bond. There was evidence of an alteration in the date of the bond. It appeared that the date had been changed from 1871 to 1873. The court held that if this alteration was made without the surety's knowledge and assent the creditor could not recover. When the principal party modifies his contract it is fatal to its validity as against the surety whose assent has not been obtained, even if it does him no harm or is actually *for his benefit*. He has a right to stand upon the very terms of his obligation, and he is not bound if any unauthorized variation is made which substitutes an agreement different from that which he agreed to. There are, however, some cases, which hold that a surety for a lessee is not discharged by a new agreement entered into without his consent, between the lessor and the lessee, reducing the rent. See also *Crompton's Estate* (1891), 9 Pa. C. C. 401, and *Bitler's Estate* (1906), 30 Super. 84.

An important example of a material change sufficient to discharge the surety from his liability is an *extension of the time of performance granted* by the creditor to the principal debtor. But the creditor's promise to extend the time must be supported by a consideration or made under seal: otherwise it is not binding on the creditor, and it will, therefore, be considered as having no effect on the surety's liability. In *Henderson v. Ardery* (1860), 36 Pa. 449, it was held that a creditor, having a principal debtor and a surety for the debtor, releases the surety by entering into a legally enforceable agreement with the principal debtor by which he extends the time of payment for any definite period beyond that mentioned in the original contract.

In *Bauschard Company v. Fidelity Company* (1902), 21 Super. 370, the court said:

"The right of the principal to postpone the fulfilment of the contract is at variance with that of the surety to demand its punctual performance or to perform it himself and sue for indemnity; and generally any act of the creditor which prevents the surety from insisting on the fulfilment of the contract as originally made, or which entitles the principal debtor to delay, is a ground of defense in an action against the surety."

In this connection note a distinction between the case of a surety and that of a guarantor. In some cases the extension of time for payment will not discharge the guarantor, unless he is injured by the extension, while it will discharge the surety. In *Follmer v. Dale* (1848), 9 Pa. 83, the owner of a house sold it to another, and a third party became guarantor for the purchase money. After the sale the seller accepted a judgment note from the buyer, payable in one year. Judgment was entered on the note at maturity, and the land was sold by the sheriff. In a suit by the seller upon the guaranty, a question was raised whether the giving time by taking a judgment note payable in one year discharged the guarantor. The court said that taking a note and entering judgment would not discharge the defendant, and whether the delay would, or would not, depended on whether he was surety or guarantor. If a surety, he was discharged, but if a guarantor, then the plaintiff may prove that no injury was done by the delay, and hold the guarantor liable. Although the original parties have no right to alter the contract to the prejudice of the guarantor, yet when it distinctly appears he has not been injured, he cannot complain.

(D) Discharge by impossibility.

This is a matter of rare occurrence and, therefore, of slight importance. The most obvious example would be a guaranty of the performance of personal services. If the party from whom performance was looked for were to die, his security would be discharged, unless otherwise expressly provided.

The death of the surety does not usually terminate his liability. His estate is bound. Generally such a question does not arise, because most contracts of suretyship provide that the surety's executors, administrators, heirs and assigns shall be bound. See *Busch's Estate* (1878), 12 Phila. 53. The act of April 11, 1848, provides that the death of one joint judgment debtor shall not release his estate from the payment of the judgment. This act applies to joint contracts; so, if a joint note is given by two and one who is a surety dies, his estate is bound.

The liability of a guarantor seems to stand upon a different footing so far as his death is concerned. In *Slagle v. Amberson* (1888), 1 Mona. 30, suit was brought on a contract guaranteeing the payment of advances to a certain third person to an amount not exceeding \$2,000. The guarantor died and the creditor, knowing of his death, made advances subsequently. It was held that the plaintiff could not recover from the guarantor's estate, because the death of the guarantor operated as a revocation of the agreement, when notice of it was communicated to the creditor. If a seller of goods takes a guaranty which is not a continuing one but a mere promise to guarantee all the debtor's bills up to a given amount, the guarantor's death revokes the guaranty, though the creditor had no knowledge of the death.

(E) *Discharge by bankruptcy.*

See Bankrupt Act, Sec. 16, and Pa. Insolvency Act, Sec. 34.

CHAPTER LI.

RIGHTS AND OBLIGATIONS OF THE PARTIES.

(A) *Obligations of creditor towards surety or guarantor.*

1. *To take action against the principal.*—A surety is directly liable under his obligation. He is an insurer of the payment of the debt, and must respond accordingly to the creditor if the debtor does not pay it. There is no necessity

for the creditor to pursue the principal debtor before he can hold the surety liable, unless the surety has given the creditor notice to proceed against the principal debtor. In *Cope v. Smith* (1822), 8 S. & R. 110, the court said that the bare omission to bring suit against the principal, will not discharge the surety. It is the business of the surety to watch the principal, and if he thinks himself in danger, to apply to the creditor, and insist on his taking measures for the recovery of the debt. When, however, a creditor makes an agreement without the consent of the surety, by which he disables himself from bringing suit, he ought not to hold the surety responsible. In *Cope v. Smith* the court said:

“Whether the principal be alive or dead, it is the business of the surety to keep an eye on his affairs, and request the creditor to bring suit, whenever he thinks himself in danger. I do not say that there may not be cases of collusion, in which the conduct of the creditor would be deemed fraudulent; but such cases would turn on a different principle.”

We have been considering the necessity of the creditor's pursuing the principal where no demand for such pursuit has been made by the surety. Take the case in which the surety gives notice to the creditor to sue the debtor, and the creditor fails to bring suit. The surety is discharged, if the creditor could have obtained his money by obeying the notice.

The surety must give a clear and explicit notice in such case. If he does not give the notice personally, but by an agent, it is prudent to give the agent written proof of his authority to act, so that such proof can be shown the creditor and the latter can have no justification for saying that he did not receive proper notice. In the notice the surety should be careful to state that unless his demand that the creditor pursue the debtor is complied with, the surety will consider himself released from all obligation in the matter. The act of May 14, 1874, provides that where a surety is bound for the forbearance or payment of money at any future time, a notice by the surety to the creditor demanding that he proceed against the debtor, must be in writing and signed by the party giving the same. A written paper must be delivered to the creditor,

and reading to a creditor a written notice to proceed against the debtor, without leaving with the creditor either the original notice or a copy of it, is not sufficient.

If the surety gives notice to the creditor to bring suit against the debtor, or to allow the surety to bring suit in the creditor's name, he does all that is necessary. In a suit against him by the creditor on his suretyship contract, the creditor, in order to excuse his failure to sue the debtor, must show that the money could not have been collected if suit had been brought when the notice was given. See *Strickler v. Burkholder* (1864), 47 Pa. 476, and *Wetzel v. Sponsler* (1852), 18 Pa. 460.

Consider the necessity of the creditor's pursuing the principal debtor where the transaction is one of *guaranty*. A guarantor is liable only for the principal debtor's ability to perform the act or make payment. The guarantor is an insurer of the solvency of the debtor, and undertakes to pay if the debtor cannot. And so, while a surety is liable in the first instance, a guarantor is not liable until the creditor has pursued the debtor and has found him insolvent and unable to pay. However, the guarantor is liable if the creditor can show that, at the time of the maturity of the debt guaranteed, the pursuit of the debtor would have been useless, because he was at that time wholly insolvent. The creditor has to do more than show merely that he demanded payment of the debtor and that payment was refused. See *Johnston v. Chapman* (1831), 3 P. & W. 18.

The creditor cannot go against the guarantor until the debtor is insolvent and cannot be made to pay; and the question arises as to how the solvency of the principal debtor is to be determined. In *Janes v. Scott* (1868), 59 Pa. 178, the court said that the test is: What might have been recovered by legal proceedings against the debtor? The fact that the debtor has a reputation for honesty and that he has in times gone by regularly paid his debts, is not sufficient to establish solvency without evidence that he has means. The word "solvency" implies ability to pay, not a mere disposition to pay.

If the creditor uses due diligence in his pursuit of the principal debtor, and is unsuccessful, he can recover against

the guarantor. In *Hoffman v. Bechtel* (1866), 52 Pa. 190, the court says:

"But what is due diligence? Perhaps it is impossible to define it with any degree of certainty. It must vary with the circumstances of each case, and hence it is a question for the jury. It cannot be less than such as a diligent creditor ordinarily employs to recover a debt for which he has no other security than the obligation of the debtor." See *Association v. Lichtenwalner* (1882), 100 Pa. 100.

Although the creditor must be diligent in looking to the principal debtor before he can hold the guarantor liable for any loss, yet the guarantor may excuse the creditor from this duty, which is imposed on the creditor for the guarantor's benefit. *Tinkum v. Duncan* (1855), 1 Grant 228.

The distinction between the contract of suretyship and that of guaranty crops out in many places. If a creditor holds collateral security and the case is one of guaranty, he is bound to use due diligence to make what he can on the security, although the guarantor does not ask him to do so. In a case of suretyship the creditor is under no obligation to realize on collateral without a special request by the surety. If the principal debtor gives securities to his surety the creditor is entitled to them. It makes no difference that he did not know of their existence when he gave credit to the debtor. *Kramer's Appeal* (1860), 37 Pa. 71.

2. *To give notice of the principal's default.*—From the very nature of the liability it appears that a surety may be called on to make good the default of the principal debtor without any notice to him of the default. He has undertaken to become bound as the principal debtor is bound and accordingly the only thing the creditor need do in order to recover from the surety is to show that the debtor has failed to do what he was bound to do.

On the other hand, in *Taylor v. McCune* (1849), 11 Pa. 460, it was stated that the neglect of the principal creditor to give the guarantor notice of the default of the party primarily liable discharges the guarantor if he can show that he has suffered actual damage from the omission. Suppose, for example, a guaranteed debtor makes default while

solvent; the creditor gives no notice to the guarantor; later the debtor becomes insolvent, and finally the creditor seeks to recover from the guarantor. The guarantor has here a valid defense to the creditor's suit, for it would be obviously unfair to hold him liable for a debt which he might have recovered had he received notice at the time of the default and before the insolvency of the debtor. If, however, the debtor is insolvent at the time of the default, no notice to the guarantor is necessary. Such notice would serve no useful purpose. See *Gibbs v. Cannon* (1823), 9 S. & R. 198. Yet prudence would suggest that it is a safer course for a creditor to give prompt notice to the guarantor in every case of the default of the debtor, in order to anticipate any possible defense of the guarantor on this ground.

(B) *Obligations of surety or guarantor towards creditor.*

The measure of the surety's or guarantor's obligations depends very largely on the obligations of the principal debtor. A surety or a guarantor is bound to no greater extent than the principal debtor or obligor: ("obligor" means a party who is bound under a legal obligation to do something). It follows, then, that in order to ascertain the extent of the liability of a surety or guarantor reference must be made to the contract between the principals. *Dunbar v. Fleisher* (1890), 137 Pa. 85. It must never be taken for granted, however, that the obligations of a surety or guarantor extend as far as those of the principal. Many creditors have learned to their cost that the courts are careful to restrict the liability of a surety or guarantor within the bounds set by the contract which he signed.

A question may arise as to how long the creditor is intended to be secured by a contract of suretyship or guaranty. Suppose, for example, the contract, signed and sealed by Richard Roe, reads, "I hereby guarantee payment of the debts of John Doe to William Smith up to \$100." How long is Richard Roe to be held under this contract? Can William Smith rely for an indefinite time on this security up to \$100? Where the contract does not mention the time for which it is to hold good, the courts presume that it is made with a particular transaction in view and that, after debts to the amount then contemplated

have been contracted, the surety or guarantor is not to be held further liable, unless the contract clearly contemplates a continuance of liability. See the three following cases:

In *Bussier v. Chew* (1862), 5 Phila. 70, it appeared that Chew had given Bussier a writing by which he agreed to become surety "for any bills contracted by Edw. Stiles from this date; said bills in the aggregate not to exceed \$300." Goods to the amount named were soon purchased and paid for. Bussier attempted to hold Chew liable for subsequent transactions, upon the theory that Chew had entered into a contract of *continuing guaranty*. The court held otherwise, and said that the guaranty was discharged as soon as Stiles had bought and paid for \$300 worth of goods.

In *Bentz's Estate* (1881), 14 Phila. 258, we have an example of a continuing obligation. Bentz agreed to assure the payment at maturity of all subsequent indebtedness of Weikel to Elliott, "hereby waiving notice of the time and amount of any future sales, and waiving also notice of non-payment on proof of demand being made. The amount recoverable on this obligation not to exceed the sum of \$500." At the time Bentz died, Weikel owed more than \$500 to Elliott for goods, but Weikel had paid Elliott more than \$500 for goods bought after Bentz had signed the agreement. At the audit of Bentz's estate, in the Orphan's Court, Elliott was allowed his claim of \$500. The court said the contract was a continuing one upon which Bentz was liable so long as Elliott sold goods to Weikel.

In *Allen v. Herman* (1859), 3 Phila. 378, it appeared that the plaintiff had leased a house and lot to another for a month, with a provision that *if the rent was paid* when it fell due, the tenant might continue in possession at the same rent from month to month, until notice to quit. The defendant had guaranteed the tenant's performance of his agreement. The tenant failed to pay the rent as agreed, but was nevertheless allowed to remain in possession of the premises. The plaintiff sought to hold the defendant liable for the rent of the ensuing month, notwithstanding the failure of the tenant to pay the rent for the month before, but the court held that the guarantor was not liable.

Every surety is liable for the whole debt, no matter how many sureties there are who are jointly bound. In *Wharton v. Duncan* (1877), 83 Pa. 40, the court said:

“A creditor may release, or compound with, or give time to one co-surety without prejudicing his right to proceed against the others; but he cannot recover from the other co-sureties more than the proportion they would have paid, supposing the co-surety released had contributed his share.”

In *Ackerman's Appeal* (1884), 106 Pa. 1, it is said that, as between themselves, each of several joint debtors is liable only for his proportion of the debt; and if one surety pays it all, he may make the others contribute towards reimbursing him. Any collateral held by one of several sureties must be used for the common benefit of them all.

(C) *Obligations of principal towards surety or guarantor.*

Where the surety has undertaken his obligation upon the principal debtor's promise to pay him a certain sum, the risk assumed by the surety is sufficient consideration to make the promise enforceable. In this part of the book, however, we shall treat only the obligations of the principal towards the surety or guarantor which arise when the latter is forced to pay the creditor. It is usually wise for a surety who is compelled to pay the principal's debt to obtain from the creditor a formal contract assigning his rights to the surety. This course, however, is seldom legally necessary to follow, for in most cases the surety who has paid the creditor becomes entitled by operation of law to the creditor's rights as against the debtor. A formal assignment should always be taken where the debtor did not request the surety to become responsible for him. Most policies of credit insurance companies, which insure the payment of mercantile accounts, contain a clause requiring such an assignment to be made.

The surety may, under some circumstances, pay a debt before it becomes due and then demand the amount so paid from the principal at maturity. In *Craig v. Craig* (1835), 5 Rawle, 91, the court said that a surety is not always bound to

subject himself to the risk of an action at law by waiting until the creditor has a right to sue him. He may look out for his own safety and take any precautions, so long as he does not sacrifice the interests of his principal. It was held that such a payment before the debt became due was not a voluntary payment, and so did not mar the surety's right to recover from the principal debtor after the debt became due.

The surety who pays the debt acquires all of the creditor's rights against the principal. It is generally stated that in such case the surety is subrogated to the creditor's rights. Anyone who steps into the surety's shoes and pays the obligation has the same rights of subrogation as the surety, provided the person so intervening was bound to pay the obligation, as for instance, where he was surety of the original surety. An important exception to this rule as to subrogation occurs where bail is given to delay an execution issued on a judgment, and to obtain what is technically known as a stay of execution. Where one becomes bail for such purpose, and is afterwards required to pay the judgment, he has no right to be substituted as plaintiff in the judgment. This would be unfair to subsequent judgment creditors of the same debtor. Before a surety has any rights of subrogation, he must pay the debt. *Forest Oil Company's Appeals* (1888), 118 Pa. 138.

A surety who pays, has a right to any collateral security held by the creditor for the protection of the debt paid by the surety. In *Hughes v. Ranken* (1869), 7 Phila. 175, the court said: "A surety is entitled to the benefit of securities given to the creditor, and it makes no difference that they are subsequent to the execution of the contract." When a surety pays a debt, the debt is usually not extinguished; the surety has the option of treating the transaction as a purchase by him of the debt and of the securities taken by the creditor to secure its payment. The surety may, however, intend to extinguish all rights under the original obligation to the detriment of his own interests; but such a state of facts must be proved. It will not be presumed. *Gossin v. Brown* (1849), 11 Pa. 527.

CHAPTER LII.

FORM OF AGREEMENT.

Creditors who are unfamiliar with legal pitfalls sometimes take an agreement of suretyship which to them seems entirely adequate, but which will not really protect them. We have seen that, in many cases, if notice is not given to the surety of something done by the creditor, either the surety never becomes bound or else he is discharged from the liability which he assumed.

If one offers himself as surety for another he is not bound until the one to whom the offer is made gives notice that he has accepted the offer. Again, if an extension of time is granted to the principal under a contract binding the creditor to postpone action, this discharges the surety who had no notice of and did not consent to the extension. Again, we have learned that often there is a question as to whether a security is continuing or not; that if it is continuing it covers future credits given by the creditor to the debtor, but if it is not, such future credits are not covered. Again, the creditor and debtor may wish to modify their agreement in some particulars without changing its substantial purpose; but this sometimes has the effect of discharging the surety, even though the alteration tends to benefit him. Again, where the creditor has any property of the debtor in his possession or control and surrenders it, the surety may be discharged wholly or in part. Then, too, the surety or guarantor may die, and if there is no express agreement as to what effect this shall have upon his liability, a question is pretty apt to be raised. In view of the above considerations, we can easily see the importance, from the creditor's standpoint, of having an agreement drawn up which will give him full protection.

No form of agreement can be drawn up which will fit all cases, for in each case its particular facts and circumstances must be referred to. It is customary in such an

agreement to begin with the provision that the principal and surety (naming them) are held and firmly bound unto the creditor or obligee (naming him), his heirs, executors, administrators and assigns, in a certain sum, which is named.

The next paragraph should contain a "Whereas" clause, setting out briefly the facts which are the basis of the creditor's claim. The paragraph following that states the condition of the obligation, and goes on to say that if the principal does the certain thing which he has bound himself to do, then the bond shall be void and of no effect; otherwise it is to be and remain in full force. If it is desired to insert any special stipulations, this may be done in succeeding paragraphs, which begin with the form, "It is further agreed—"

The following Form of Agreement may be useful in ordinary mercantile transactions:

KNOW ALL MEN BY THESE PRESENTS, That we, James Coe, of the City of Philadelphia, principal and John Doe [or an Indemnity Company as the case may be, in which case it should be stated that it is a corporation of the State of] of the said city, as surety, are held and firmly bound unto Richard Roe, of the said city, in the sum of Ten Thousand Dollars (\$10,000), lawful money of the United States of America, to be paid to the said Richard Roe, his heirs, executors, administrators, or assigns, to which payment well and truly to be made we do bind and oblige ourselves, our heirs, executors, and administrators [or successors if the surety is a corporation], and every one of them, firmly by these presents.

Sealed with our seals, dated the day of, in the year of our Lord one thousand nine hundred and (190..).

WHEREAS, The said Richard Roe is about to allow the said James Coe a line of credit for merchandise, for the payment whereof the said John Doe has agreed to become surety,

Now the condition of this obligation is such that if the said James Coe shall punctually pay the said Richard Roe for all merchandise which he shall purchase, according to the terms upon which the same shall be bought, then this obligation to be void; otherwise to be and remain in full force and virtue.

IT IS FURTHER AGREED, That the above contract of suretyship shall be subject to the following provisions:

First. No notice of the granting of credit by the said Richard Roe to the said James Coe need be given to the said John Doe in order to render the latter liable on this obligation.

Second. The liability of the said John Doe shall apply to all future grants of credit up to a total indebtedness of Five Thousand Dollars (\$5,000). Such grants of credit not to extend over a period of more than two years from the date hereof. This agreement shall not be taken to restrict the right of Richard Roe to allow James Coe credit beyond the sum of \$5,000.

Third. The said Richard Roe may grant extensions of time to the said James Coe, either with or without consideration, and may accept or surrender any notes and other collateral, without giving notice thereof to the said John Doe, and without releasing him in the least from this obligation.

Fourth. The said Richard Roe shall not be obliged to give notice of any sort to the said John Doe until he desires him to make payment in pursuance of his obligation under this agreement.

[Signed] , Surety. (Seal)
[Signed] , Principal. (Seal)

Sealed and delivered in
the presence of
.....
.....

PART II

INSURANCE

CHAPTER LIII.

FIRE INSURANCE.

(A) Who has an insurable interest.

The very nature of the contract of insurance on property, makes it necessary that the insured have some interest in the property, either as owner or in some other capacity. An owner of property can always insure it, and, when a loss occurs, recover up to the full value of the property, provided the amount of the policy is as large as the value of the property. Likewise one who has a specific lien on property, such as that held by a mortgagee, may insure and recover to the full extent, because his interest will be adversely affected by the loss of the property.

One who is under a liability to care for property, and who will suffer loss in case of its destruction, has an insurable interest in it. For instance, a common carrier is an insurer of property which he carries, unless he stipulates against such liability, and hence he may insure and recover to the full extent of the value of the property. A bailee of goods frequently insures them to protect himself from losing his charges upon them in case of their loss, or to protect him from being forced to pay the value of them to the bailor in case they are lost because of their being stored in an unsafe place. A trustee of either real or personal property, who is under a duty to see that the property is carefully preserved, has an interest upon which to base a contract of insurance, for, in many cases, if he fails to insure and the property is lost, he will personally have to stand the ultimate loss.

On the question of insurable interest, see *Sweeny v. Franklin Fire Ins. Co.* (1853), 20 Pa. 337. In that case a party of squatters entered upon a piece of ground near Lewes, Delaware, and built a hotel. The land belonged to the State of Delaware, and the squatters had no title whatever to it. The man who built the hotel accepted from his associates a conveyance of the building in payment of his claim for doing the work. He then took out a policy of insurance, and afterwards the hotel was destroyed by fire. In a suit upon the policy it was held that the plaintiff could not recover, because he had no insurable interest. The facts that he was in possession and had a conveyance from the people for whom he erected the building, were immaterial. Where a man, without any right to do so, builds a house upon land belonging to another man, the house becomes the property of the owner of the land.

In *Western and Atlantic Pipe Lines v. Home Ins. Co.* (1891), 145 Pa. 346, it appeared that the Pipe Line Company had contracts with its customers requiring it to protect by insurance their oil while in the company's tanks. The company took out a policy on the oil, the policy being issued to it as owner. In a suit on the policy it was held that the company had an insurable interest in the oil and might recover.

If a man enters into a contract of sale whereby he agrees to sell certain land to another, each party has an interest to protect. The vendor is still the owner, because he has not yet conveyed the legal title. The vendee is bound to take the property and pay the purchase price, even though the buildings are destroyed by fire, unless he protects himself by proper stipulation in the contract of sale. Frequently, in the case of personal property, one who has the possession of them insures "for whom it may concern." In such case this gives him the right to recover the full value of the goods in case of loss, and if he is not the absolute owner, he holds as trustee for any other party in interest. Both the vendor and the vendee in a contract of sale of personal property, have an insurable interest therein.

In *Burson v. Fire Association of Phila.* (1890), 136 Pa. 267, property was sold under an instalment lease. The sale was conditional, because the vendor reserved to himself the title until the last payment should be made. Later he procured a policy of insurance upon the property. In a suit upon the policy, it was held that the vendor had an insurable interest. He was the sole and unconditional owner of the property within the meaning of the policy, because he was responsible to the vendee, either for the property or the amount paid. He was allowed to recover the full value of the property without any deduction for the amount paid by the vendee. The court said that the insurance company had no standing to defend upon the ground that as to the vendee's creditors the agreement of sale was fraudulent in law. See Chapter XL for a discussion of instalment contracts.

A mortgagee has an insurable interest in the mortgaged property, because if it is destroyed his security is lost. A judgment creditor has no insurable interest in his debtor's property, although the judgment was given for purchase money. The courts distinguish the cases by saying that the mortgagee has a specific lien upon the mortgaged property, while a judgment creditor has only a general lien upon all of the debtor's real estate in the county where the judgment is entered. The practical importance of this distinction is, that when a man sells a piece of real estate upon which there are building improvements, it is much safer for him to take a mortgage for the unpaid purchase money than to take a judgment note; for then he puts himself in a position to insure the property and protect himself from losing what may be his only valuable security.

A lessee has an insurable interest in the leased premises, the lease binds him, no matter what happens, to return the property in good order and condition at the end of his term. In such case he may insure and recover to the full value of the property. *Ins. Co. v. Murray* (1873), 73 Pa. 13.

A partner has an insurable interest in the entire firm stock. If a loss occurs, he must account to the firm on receiving payment from the insurance company.

There are many cases in which a man is merely a life tenant of property which he occupies; that is to say, upon his death the property goes to somebody else, irrespective of the life tenant's will. Although a contract of property insurance is based upon the idea of indemnity, and the insured cannot recover more than his actual loss, yet a life tenant may insure in his own name and recover for the entire value of the property, in case of total loss, unless he insures merely his own interest in the premises. Any other rule would be very inconvenient, because, although a life interest in real estate is roughly estimated to be worth about one-third of the value of the property, it would be impracticable for a life tenant to rebuild only one-third of a dwelling or any other structure. He is entitled to the entire possession while he lives, and so he is allowed to recover to the full value of the property, if the amount of the policy is as large as that, and then he stands as a trustee for the amount recovered in excess of his interest.

A widow has an insurable interest in realty out of which her dower is payable. A husband has an insurable interest in his wife's real estate during her life. Where a wife purchases real estate and takes possession with her husband, the husband has an insurable interest upon which he may take out a policy in his own name, even though a conveyance has not yet been made to the wife of the legal title. His interest is said to be based partly upon his rights as tenant by curtesy. It is wise, nevertheless, to take out insurance in the husband's name, if he owns the property, and in the wife's name if she is the owner. *Study the terms of your policy in all these matters, for it may settle the disputed question!*

In *Diffenbaugh v. Union Fire Ins. Co.* (1892), 150 Pa. 270, the husband insured goods in his name, as owner, though the title was in his wife. In a suit on the policy to recover for a loss, there was no offer to show that when the company wrote the policy they were informed of the fact that the property belonged to the wife. The court refused to allow the real owner to prove by her husband that he was acting as her agent when he made the application for the

insurance to the agent of the company. The policy contained a clause rendering it void if the interest of the insured was not truly stated therein. The court stated that such a clause in the policy was intended to enable the company to know whom it was insuring. The plaintiff was non-suited.

An agent or consignee who holds his principal's property is responsible for it. He has a pecuniary interest in it to the amount of his commissions. He may insure it in his own name, and if it is destroyed he may recover the full value of the property if that does not exceed the amount of the policy. He holds the insurance money in trust for his employer to the extent that this money exceeds his own interest in the property. *Roberts v. Firemen's Ins. Co.* (1894), 165 Pa. 55.

It is not necessary that the plaintiff should have an interest at the time of taking out the policy. It is sufficient if he acquires his interest at any time during the running of the policy and before the loss. As a practical matter, an insurance company will seldom issue a policy to one who has no interest in the property at the date of the policy. What is termed the "moral hazard" is too great. Even though an interest at the date of the loss is sufficient, yet generally an insurance company is not willing to take the risk of insuring a man who has no interest in the property at the time and who may, after effecting insurance, acquire an interest and burn the property.

In the case of property insurance, *interest must exist at the time of the loss*; but when we come to consider life insurance, we will see that it is sufficient if there is an interest at the time of the issuing of the policy.

(B). *Formation of the contract.*

In Pennsylvania we have an act of assembly forbidding private individuals to act as insurers against fire and lightning. Insurance policies on property cannot lawfully be issued except by corporations. There are, besides, certain statutory restrictions on the doing of business by foreign insurance companies.

In contracting with a mutual company, it is important for the insured to live up to the provisions of the by-laws

of the company. In the case of *Schaffer v. Mutual Fire Ins. Co.* (1879), 89 Pa. 296, it was proved that the by-laws of the company required every person applying for membership to pay a certain fee and a premium, and to sign the policy. A person desiring insurance called upon the company's secretary for the purpose of getting a fire policy on his dwelling house. The secretary agreed to accept the risk and the policy was prepared. The applicant was enrolled on the company's books as a member, but he did not sign the policy or make the required payments. The property was destroyed by fire the next morning and the company refused to deliver the policy to the owner. In a suit against the company the plaintiff testified that he had agreed to make the payments when he received the policy, but the court held that a contract had not been consummated; and judgment was given for the defendant.

The act of May 11, 1881, provides that "all life and fire insurance policies upon the lives or property of persons within this Commonwealth, whether issued by companies organized under the laws of this State or by foreign companies doing business therein, which contain any reference to the application of the insured or the constitution, by-laws or other rules of the company, either as forming part of the policy or contract between the parties thereto, or having any bearing on said contract, shall contain, or have attached to said policies, correct copies of the application, as signed by the applicant, and the by-laws referred to; and, unless so attached and accompanying the policy, no such application, constitution or by-laws shall be received in evidence in any controversy between the parties to, or interested in the said policy, nor shall such application or by-laws be considered a part of the policy or contract between such parties."

Where a company properly executes a policy and delivers it to the insured or his agent, the contract is completed by such delivery, there being no stipulation in the policy making actual payment of the premium a necessary prerequisite to completion of the contract, and there being no provision that default in the payment of the premium shall

constitute a forfeiture. In such case actual pre-payment of the premium is not necessary in order to make a valid contract. In fire insurance, the first premium is generally the whole consideration received by the insurer. But in some cases the danger of loss may be increased with the consent of the insurer, who is then entitled to charge an additional premium.

An insurance company has a right to insist upon the payment of the premium before it delivers the policy, and the contract is not complete where the company refuses to make delivery on such ground. A contract of insurance may be made, however, although no policy is ever issued. If all the requisites of a contract are present the contract is binding on both parties. Where the charter of the company provides that the contract shall be in writing, a verbal contract does not bind the company unless it has accepted a premium, or unless there are other facts which make it inequitable for the company to defend upon the ground that the contract is not in writing.

The question often arises whether or not payment of the first premium has been made in such a way as to make the policy binding. The company is bound as soon as its duly authorized agent accepts a premium tendered to him. Such payment is a payment to the company. Where a company executes a policy and delivers it to a person to deliver it to the insured, the policy containing a receipt for the first premium, it thereby makes the person to whom the policy is delivered its agent to deliver the policy to the insured and accept the premium from him. In such case, if the insured gets the policy after paying the premium, the company is bound, notwithstanding a condition in the policy that it shall be void if the insured neglects to pay the premium directly to the company. *Lebanon Ins. Co. v. Erb* (1886), 112 Pa. 149.

Usually a fire policy does not require pre-payment of the first premium as a condition of the company's becoming bound. In such case, if the agent delivers the policy, it will be presumed that he had authority to do so, and that it was to go into effect upon such delivery.

(C) Reality of consent.

If the insured has an insurable interest, and the policy does not require him to make a statement of that interest he need not make such statement to the company. Generally the company requires such statement. The applicant for an insurance policy is under a duty to answer all questions put to him in his application, and to answer them fairly, candidly and fully. An applicant for insurance may know of a particular fact but he may not know that it will increase the risk. In such a case he is not bound to inform the company of such fact, although there is a warranty in the policy that the insured has not omitted to state information material to the risk. If the insured had reason to believe that the company would regard the fact as a material increase of the risk, that would change the situation.

Even though the insurance company does not rely upon the applicant's representation in issuing the policy, but upon its own knowledge of the nature of the risk, the policy is void if the applicant conceals information of matters tending to increase the risk. *Cumberland Co. v. Schell* (1857), 29 Pa. 31. For instance, if an applicant for insurance knows that a malicious attempt has been made to set fire to his house, and conceals this fact from the company, the company is not liable in case of loss.

A warranty is a vital, binding representation as to a fact. Whether or not the fact would be material if there were no warranty, the parties, by treating it as a warranty, make it material. If the fact is not as warranted, the policy is avoided. It does not make any difference in such a case whether or not the insured is innocently mistaken; he is bound by the warranty. On the other hand, a mere misrepresentation, made in good faith, does not avoid a policy unless it is material.

When we come to consider life insurance we will see that there is a statute providing that a warranty shall not avoid a life policy unless the matter is of actual importance. Representations in a policy are construed to be warranties only

where they have a tendency to induce the company to enter into a contract on terms more favorable to the insured than otherwise it would allow. There can be no recovery upon a policy where the insured represented that the property was owned by a successful business man, it appearing in fact that the title was in a married woman. *Freedman v. Fire Association* (1895), 168 Pa. 249. If the policy provides that any description referred to in it shall be a part of the contract and warranted by the insured, he should be careful to designate the property correctly as a dwelling house or whatever it may be. The company has a right to have truthful answers to the question whether or not the property is encumbered, and may also provide that the policy shall be avoided by future encumbrances unless the consent of the company is obtained. If the company cancels the policy in such case, it must repay a proportionate part of the premium.

(D) Conduct of insured after policy is issued.

Where the insured says in his application, in answer to the question therein put to him, that there is a watchman on the premises when the property is not in use, this constitutes an agreement to keep a watchman, and the insured must comply with it. Where a man is going to vacate his property for a time, as, for instance, where he is going to leave it unoccupied for the summer, he should get the company to consent to this by pasting a "rider" upon the policy, agreeing to a temporary vacancy. A provision that a policy on a manufacturing establishment shall become void if operations are ceased will be binding provided the establishment was in operation when the insurance was effected.

Most policies provide that they shall become void if the insured brings dynamite, gunpowder, or other dangerous articles upon the premises. The insured must be careful about these matters or he will lose his right to recover for loss.

Another important provision in most policies is that any transfer of the property, without the company's consent, shall avoid it. The transfer referred to means a change of

interest after the date of the insurance. The transfer of the property by operation of law, upon the death of the insured, is not within the clause against alienation.

Most policies provide that the insured shall not increase the risk without the company's consent. The condition that if the hazard be increased by any means within the control or knowledge of the insured the entire policy shall be void, is meant to protect the company where there is a change in structure, methods of heating, or the addition of new buildings. *Collins v. Assurance Corporation* (1895), 165 Pa. 298. The company does not have to pay, *although the fire does not result from the increase of risk*, where the insured has in fact increased the risk contrary to the provision of the policy.

A provision in the policy that the placing of additional insurance shall avoid the policy unless the insurer has notice, was upheld in *Bard v. Ins. Co.* (1893), 153 Pa. 257. Where there is no stipulation against additional insurance, and other insurance is taken out upon the same risk, the respective insurance companies are liable *pro rata*, all the policies being considered as one policy. *Clarke v. Assurance Co.* (1892), 146 Pa. 561.

If the insurance company knows of a violation of a condition against additional insurance and continues to treat the policy as valid, it thereby waives the breach of condition. Incidentally it may be remarked that other breaches of condition may be waived in the same manner. The insured, however, must not rely upon the knowledge of a mere agent and his acceptance of premiums under such circumstances, because generally an agent has no power to waive a breach of condition.

(E) *What risks are covered.*

Where the insured does not act fraudulently, a fire policy protects him against fire caused by his own ordinary negligence. But if he acts fraudulently, or if his negligence is gross or reckless, he cannot recover on his fire policy if the loss results from such fraud or gross negligence. A fire policy protects not only against loss by fire, but also against

loss following as a natural consequence of the fire. For instance, where a man removes goods from a burning building, or from a building *adjoining* a burning building, and the goods are lost or stolen by reason of the removal, the owner is entitled to recover under a fire policy, if he had reasonable grounds for thinking that this measure was necessary to save the goods from destruction. Again, loss caused by water used to extinguish a fire is covered by the policy.

Another loss covered by a fire policy is that resulting from the falling of walls of a neighboring building which has been destroyed by fire. In such case, if the walls fall during the fire, or soon thereafter, the damage done by their falling is held to be covered by a fire policy. An owner of insured property which catches fire and is in the course of sure destruction, may blow the property up with gunpowder to prevent the fire from spreading. In such case the company is liable. *Greenwald v. Ins. Co.* (1859), 3 Phila. 323.

In *Fire Association v. Williamson* (1856), 26 Pa. 196, a man owned adjoining buildings which he had rented out to different tenants. He insured them in one policy for a certain sum on each. The policy provided that it should be avoided if gunpowder was kept on the premises without the knowledge and consent of the company. One of the tenants ran a store in which he kept gunpowder. Neither the company nor the landlord knew of this. The gunpowder exploded and caused a fire which destroyed all the buildings. No recovery was allowed against the company because the contract was an entire and indivisible contract.

(F) *Transfer of policies.*

Consider the every-day transaction in which there is a contract to sell real estate that is covered by a policy of insurance taken out by the owner. Suppose that the contract of sale says nothing about the policy of insurance and the owner of the property executes the deed to the purchaser. The property then burns down. The vendor cannot recover on his policy of insurance because he has not lost anything. He has his purchase money and is no longer the

owner of the property. The vendee cannot recover because he has never made a contract with the company. This shows how important it is, if you are the purchaser in such case, to stipulate for a transfer of the policy at the time of the completion of the sale and the delivery of the deed. The consent of the company to such transfer is generally easy to obtain.

Suppose a case in which the owner of insured property gives a mortgage on it. The mortgagee wants to be protected in case of loss by fire, and so the parties get the company to attach a "rider" providing "loss, if any, payable to the mortgagee." This protects the mortgagee in case of loss, unless the mortgagor has done some act which gives the company the right to forfeit the policy. But, as a business matter, the mortgagee wants to be protected notwithstanding any act of forfeiture by the mortgagor. In order to meet this situation, the company attaches to the policy a "rider" containing not only the above quoted provision but further, that if the company shall claim that the mortgagor has committed any act giving the company the right to forfeit the policy, the company will, nevertheless, pay the mortgagee his loss in case of fire, whereupon the mortgagee shall assign to the company his rights under the mortgage. The form of this "mortgagee clause" is set out in full in the following chapter. The effect of this may be shown as follows: If property is worth \$10,000, and is insured for that amount by the owner, and then the owner mortgages it for \$5,000, and the company attaches the "mortgagee clause" to the policy, the rights of the parties are adjusted thus: in case of loss, where the mortgagor has not committed any act of forfeiture, the mortgagee collects the whole \$10,000, reimburses himself, and pays the balance to the mortgagor. But if the company claims that the mortgagor has committed an act of forfeiture, payment of the mortgage debt, namely \$5,000, is made to the mortgagee, and the company is then subrogated to his rights under the mortgage.

After loss, a policy of insurance is a right of action against the company and may be assigned without the consent of the company. And so, any condition against the assign-

ment of the policy after loss, without the consent of the company, is void. But the company has a right to stipulate for notice of an assignment of the policy before loss, and it may usually refuse to recognize the assignment and cancel the policy in accordance with the terms thereof. In some cases its right to refuse to approve the transfer is limited. A fire insurance company has no right to refuse to approve the assignment of a perpetual policy to the purchaser from the original insured, provided the moral hazard will not be increased by the transfer, unless there is a clause in the policy giving it such a right. If the assignee is a person of good financial standing, good habits of life, and good moral character, the company has no right to refuse to approve of the transfer. *Marshall v. Ins. Co.* (1896), 176 Pa. 628.

(G) Notice and proofs of loss.

The act of June 27, 1883, provides that the insured may furnish notice of loss within ten days and preliminary proof of loss within twenty days after the fire. This act is for the protection of the insured and does not require him to furnish the notice or proofs within said periods. A requirement in the policy that notice of loss shall be given to the company within a fixed time, say twelve days, is no basis for a forfeiture where notice is not given in such time, unless the policy makes that express stipulation. In such case, all that is required of the insured is that he give notice within a reasonable time after he knows of the loss. Many policies require notice "forthwith" upon the happening of the loss; this requirement is subject to the terms of the act of 1883. Notice within eleven days after the loss, has been held to be so late that the insured was bound to explain the delay, and give a sufficient reason for it. Notwithstanding the statement made by the insured in his proof of loss, he may, in a suit upon the policy, recover upon a higher valuation if he can prove it. But, if the insured with full knowledge swears to false proofs of loss the policy is forfeited by his fraud.

Where an insured building or a specific article of *personal property* is totally destroyed, notice of the total loss is all that

the insured need give, where the policy merely requires that a particular statement of the loss shall be given. Where, however, the policy provides that notice of the loss shall be given to the company, and that the insured shall render a particular account and proof thereof, stating the actual cash value of the property, the amount of other insurance, and the plan and specifications of buildings destroyed, the company is entitled to a particular account and proof, although the loss is a total one. *Ins. Co. v. Hocking* (1887), 115 Pa. 398.

The company may waive notice and proofs of loss. If it does this, either expressly or by implication, and gives the insured good reason to believe that it does not intend to insist upon such notice and proofs, he is not bound to furnish them. Where the insured furnishes proofs of loss in good faith which he believes to be sufficient, but which in fact contain some defects, the company is bound to make objections promptly if it intends to rely upon such defects. If the company says nothing about it, it is reasonable for the insured to suppose that he has satisfied the requirements. However, if proofs of loss are furnished after the expiration of the prescribed time, the mere fact that the company keeps them without objection does not amount to a waiver.

See as to proofs of death in the case of *life insurance*, *Baldi v. Ins. Co.* (1906), 30 Super. 213, and *Rondinella v. Ins. Co.* (1906), 30 Super. 323.

(H) *Rights of insurance company against incendiary and others.*

Under the "mortgagee clause," if an insurance company pays a loss to a mortgagee, it is entitled to be subrogated to his rights under the mortgage in certain cases. Now suppose your house burns down as the direct result of a wrongful act committed by another. This would give you a right of action against the wrongdoer. If the company pays you, it takes your right of action against the wrongdoer. In other words, the company is subrogated to your rights. See *Showalter v. Ins. Co.* (1897), 3 Super. 448, and *Ins. Co. v. Showalter* (1897), 3 Super. 452.

CHAPTER LIV.

FORM OF FIRE POLICY, AND MORTGAGEE CLAUSE.

The following is a form of fire insurance policy used in Pennsylvania:

[*Name of the Insurance Company.*]

IN CONSIDERATION of the stipulations herein named and of
dollars premium does insure (*name of insured*) for the term of
 from the day of 190., at noon,
 to the day of 190., at noon, against all direct loss
 or damage by fire, except as hereinafter provided, to an amount not
 exceeding dollars, to the following described property,
 while located and contained as described herein, and not elsewhere, to wit:

[*Description of property.*]

This company shall not be liable beyond the actual cash value of the property at the time any loss or damage occurs, and the loss or damage shall be ascertained or estimated according to such actual cash value, with proper deduction for depreciation howsoever caused, and shall in no event exceed what it would then cost the insured to repair or replace the same with material of like kind and quality; said ascertainment or estimate shall be made by the insured and this company, or, if they differ, then by appraisers, as hereinafter provided; and, the amount of loss or damage having been thus determined, the sum for which this company is liable pursuant to this policy shall be payable sixty days after due notice, ascertainment, estimate, and satisfactory proof of the loss have been received by this company in accordance with the terms of this policy. It shall be optional, however, with this company to take all, or any part, of the articles at such ascertained or appraised value, and also to repair, rebuild, or replace the property lost or damaged with other of like kind and quality within a reasonable time on giving notice, within thirty days after the receipt of the proof herein required, of its intention so to do; but there can be no abandonment to this company of the property described.

This entire policy shall be void if the insured has concealed or misrepresented, in writing or otherwise, any material fact or circumstance concerning this insurance or the subject thereof; or if the interest of the insured in the property be not truly stated herein; or in case of any fraud or false swearing by the insured touching any matter relating to this insurance or the subject thereof, whether before or after a loss.

This entire policy, unless otherwise provided by agreement indorsed hereon or added hereto, shall be void if the insured now has or shall hereafter make or procure any other contract of insurance, whether valid or not, on property covered in whole or in part by this policy; or if the

subject of insurance be a manufacturing establishment and it be operated in whole or in part at night later than ten o'clock, or if it cease to be operated for more than ten consecutive days; or if the hazard be increased by any means within the control or knowledge of the insured; or if mechanics be employed in building, altering, or repairing the within described premises for more than fifteen days at any one time; or if the interest of the insured be other than unconditional and sole ownership; or if the subject of insurance be a building on ground not owned by the insured in fee-simple; or if the subject of insurance be personal property and be or become incumbered by a chattel mortgage; or if, with the knowledge of the insured, foreclosure proceedings be commenced or notice given of sale of any property covered by this policy by virtue of any mortgage or trust deed; or if any change, other than by the death of an insured, take place in the interest, title, or possession of the subject of insurance (except change of occupants without increase of hazard) whether by legal process or judgment or by voluntary act of the insured, or otherwise; or if this policy be assigned before a loss; or if illuminating gas or vapor be generated in the described building (or adjacent thereto) for use therein; or if (any usage or custom of trade or manufacture to the contrary notwithstanding) there be kept, used, or allowed on the above described premises, benzine, benzole, dynamite, ether, fireworks, gasoline, greek fire, gunpowder exceeding twenty-five pounds in quantity, naphtha, nitro-glycerine or other explosives, phosphorus, or petroleum or any of its products of greater inflammability than kerosene oil of the United States standard, (which last may be used for lights and kept for sale according to law but in quantities not exceeding five barrels, provided it be drawn and lamps filled by daylight or at a distance not less than ten feet from artificial light); or if a building herein described, whether intended for occupancy by owner or tenant, be or become vacant or unoccupied and so remain for ten days.

This company shall not be liable for loss caused directly or indirectly by invasion, insurrection, riot, civil war or commotion, or military or usurped power, or by order of any civil authority; or by theft; or by neglect of the insured to use all reasonable means to save and preserve the property at and after a fire or when the property is endangered by fire in neighboring premises; or (unless fire ensues, and, in that event, for the damage by fire only) by explosion of any kind, or lightning; but liability for direct damage by lightning may be assumed by specific agreement hereon.

If a building or any part thereof fall, except as the result of fire, all insurance by this policy on such building or its contents shall immediately cease.

This company shall not be liable for loss to accounts, bills, currency, deeds, evidences of debt, money, notes, or securities; nor, unless liability is specifically assumed hereon, for loss to awnings, bullion, casts, curiosities, drawings, dies, implements, jewels, manuscripts, medals, models, pat-

terns, pictures, scientific apparatus, signs, store or office furniture or fixtures, sculpture, tools, or property held on storage or for repairs; nor, beyond the actual value destroyed by fire, for loss occasioned by ordinance or law regulating construction or repair of buildings, or by interruption of business, manufacturing processes, or otherwise; nor for any greater proportion of the value of plate glass, frescoes, and decorations than that which this policy shall bear to the whole insurance on the building described.

If an application, survey, plan, or description of property be referred to in this policy it shall be a part of this contract and a warranty by the insured.

In any matter relating to this insurance no person, unless duly authorized in writing, shall be deemed the agent of this company.

This policy may by a renewal be continued under the original stipulations, in consideration of premium for the renewed term, provided that any increase of hazard must be made known to this company at the time of renewal or this policy shall be void.

This policy shall be cancelled at any time at the request of the insured; or by the company by giving five days' notice of such cancellation. If this policy shall be cancelled as hereinbefore provided, or become void or cease, the premium having been actually paid, the unearned portion shall be returned on surrender of this policy or last renewal, this company retaining the customary short rate; except that when this policy is cancelled by this company by giving notice it shall retain only the *pro rata* premium.

If, with the consent of this company, an interest under this policy shall exist in favor of a mortgagee or of any person or corporation having an interest in the subject of insurance other than the interest of the insured as described herein, the conditions hereinbefore contained shall apply in the manner expressed in such provisions and conditions of insurance relating to such interest as shall be written upon, attached, or appended hereto.

If property covered by this policy is so endangered by fire as to require removal to a place of safety, and is so removed, that part of this policy in excess of its proportion of any loss and of the value of property remaining in the original location, shall, for the ensuing five days only, cover the property so removed in the new location; if removed to more than one location, such excess of this policy shall cover therein for such five days in the proportion that the value in any one such new location bears to the value in all such new locations; but this company shall not, in any case of removal, whether to one or more locations, be liable beyond the proportion that the amount hereby insured shall bear to the total insurance on the whole property at the time of fire, whether the same cover in new location or not.

If fire occur the insured shall give immediate notice of any loss thereby in writing to this company, protect the property from further damage, forthwith separate the damaged and undamaged personal property, put

it in the best possible order, make a complete inventory of the same, stating the quantity and cost of each article and the amount claimed thereon; and, within sixty days after the fire, unless such time is extended in writing by this company, shall render a statement to this company, signed and sworn to by said insured, stating the knowledge and belief of the insured as to the time and origin of the fire; the interest of the insured and of all others in the property; the cash value of each item thereof and the amount of loss thereon; all incumbrances thereon; all other insurance, whether valid or not, covering any of said property; and a copy of all the descriptions and schedules in all policies; any changes in the title, use, occupation, location, possession, or exposures of said property since the issuing of this policy; by whom and for what purpose any building herein described and the several parts hereof were occupied at the time of fire; and shall furnish, if required, verified plans and specifications of any building, fixtures, or machinery destroyed or damaged; and shall also, if required, furnish a certificate of the Magistrate or Notary Public (not interested in the claim as a creditor or otherwise, nor related to the insured) living nearest the place of fire, stating that he has examined the circumstances and believes the insured has honestly sustained loss to the amount that such magistrate or notary public shall certify.

The insured, as often as required, shall exhibit to any person designated by this company all that remains of any property herein described, and submit to examinations under oath by any person named by this company, and subscribe the same; and, as often as required, shall produce for examination all books of account, bills, invoices, and other vouchers, or certified copies thereof if originals be lost, at such reasonable place as may be designated by this company or its representative, and shall permit extracts and copies thereof to be made.

In the event of disagreement as to the amount of loss the same shall, as above provided, be ascertained by two competent and disinterested appraisers, the insured and this company each selecting one, and the two so chosen shall first select a competent and disinterested umpire; the appraisers together shall then estimate and appraise the loss, stating separately sound value and damage, and, failing to agree, shall submit their differences to the umpire; and the award in writing of any two shall determine the amount of such loss; the parties thereto shall pay the appraiser respectively selected by them and shall bear equally the expenses of the appraisal and umpire.

This company shall not be held to have waived any provision or condition of this policy or any forfeiture thereof by any requirement, act, or proceeding on its part relating to the appraisal or to any examination herein provided for; and the loss shall not become payable until sixty days after the notice, ascertainment, estimate, and satisfactory proof of the loss herein required have been received by this company, including an award by appraisers when appraisal has been required.

This company shall not be liable under this policy for a greater proportion of any loss on the described property, or for loss by and expense of removal from premises endangered by fire, than the amount hereby insured shall bear to the whole insurance, whether valid or not, or by solvent or insolvent insurers, covering such property, and the extent of the application of the insurance under this policy or of the contribution to be made by this company in case of loss, may be provided for by agreement or condition written hereon or attached or appended hereto. Liability for re-insurance shall be as specifically agreed hereon.

If this company shall claim that the fire was caused by the act or neglect of any person or corporation, private or municipal, this company shall, on payment of the loss, be subrogated to the extent of such payment to all right of recovery by the insured for the loss resulting therefrom, and such right shall be assigned to this company by the insured on receiving such payment.

No suit or action on this policy, for the recovery of any claim, shall be sustainable in any court of law or equity until after full compliance by the insured with all the foregoing requirements, nor unless commenced within twelve months next after the fire.

Wherever in this policy the word "insured" occurs, it shall be held to include the legal representative of the insured, and wherever the word "loss" occurs, it shall be deemed the equivalent of "loss or damage."

If this policy be made by a mutual or other company having special regulations lawfully applicable to its organization, membership, policies or contracts of insurance, such regulations shall apply to and form a part of this policy as the same may be written or printed upon, attached, or appended hereto.

This policy is made and accepted subject to the foregoing stipulations and conditions, together with such other provisions, agreements, or conditions as may be indorsed hereon or added hereto, and no officer, agent, or other representative of this company shall have power to waive any provision or condition of this policy except such as by the terms of this policy may be the subject of agreement indorsed hereon or added hereto, and as to such provisions and conditions no officer, agent, or representative shall have such power or be deemed or held to have waived such provisions or conditions unless such waiver, if any, shall be written upon or attached hereto, nor shall any privilege or permission affecting the insurance under this policy exist or be claimed by the insured unless so written or attached.

IN WITNESS WHEREOF, this policy has been signed by the company's agent at, acting under a power of attorney, or commission of authority (as the case may be).

Dated in, this day of, 190...

(Signature).....

Manager.

Examined. (Signature).....

Agent for the Company.

The following is a form of "mortgagee clause" in general use:

Mortgagee Clause with Full Contribution.

Loss or damage, if any, under this policy, shall be payable to as mortgagee, [or trustee] as interest may appear, and this insurance, as to the interest of the mortgagee [or trustee] only therein, shall not be invalidated by any act or neglect of the mortgagor or owner of the within described property, nor by any foreclosure or other proceedings or notice of sale relating to the property, nor by any change in the title or ownership of the property, nor by the occupation of the premises for purposes more hazardous than are permitted by this policy; PROVIDED, that in case the mortgagor or owner shall neglect to pay any premium due under this policy, the mortgagee [or trustee] shall, on demand, pay the same.

PROVIDED also, that the mortgagee [or trustee] shall notify this company of any change of ownership or occupancy or increase of hazard which shall come to the knowledge of said mortgagee [or trustee] and, unless permitted by this policy, it shall be noted thereon and the mortgagee [or trustee] shall, on demand, pay the premium for such increased hazard for the term of the use thereof; otherwise this policy shall be null and void.

This company reserves the right to cancel this policy at any time as provided by its terms, but in such case this policy shall continue in force for the benefit only of the mortgagee [or trustee] for ten days after notice to the mortgagee [or trustee] of such cancellation and shall then cease, and this company shall have the right, on like notice, to cancel this agreement.

In case of any other insurance upon the within described property this company shall not be liable under this policy for a greater proportion of any loss or damage sustained than the sum hereby insured bears to the whole amount of insurance on said property, issued to or held by any party or parties having an insurable interest therein, whether as owner, mortgagee or otherwise.

Whenever this company shall pay the mortgagee [or trustee] any sum for loss or damage under this policy and shall claim that, as to the mortgagor or owner, no liability therefore existed, this company shall, to the extent of such payment, be thereupon legally subrogated to all the rights of the party to whom such payment shall be made, under all securities held as collateral to the mortgage debt, or may at its option, pay to the mortgagee [or trustee] the whole principal due or to grow due on the mortgage with interest, and shall thereupon receive a full assignment and transfer of the mortgage and of all such other securities; but no sub-

rogation shall impair the right of the mortgagee [or trustee] to recover the full amount of claim.

Dated,

Attached to and forming part of Policy No.

.....Agent

CHAPTER LV.

LIFE INSURANCE.

What was said about the formation of the contract and the construction of the policy in property insurance is generally applicable to life insurance. In the discussion of parties, we found that only corporations can issue fire policies. But it is an open question whether private individuals can issue life policies. There is no statute against it, but the Insurance Commissioner will not license such business by private persons, there being no judicial decision requiring him to do so. See *Unincorporated Insurance Business* (1905), 32 Pa. C. C. 35. There are many unincorporated beneficial societies, but they do not do business for profit. Under the corporation act of April 29, 1874, beneficial societies are incorporated by the court as corporations not for profit. Under the act of April 28, 1903, such associations are incorporated "in the manner provided by law for the incorporation of insurance companies," but are not permitted to issue life policies for more than \$250.

The failure to pay the first premium in the case of life insurance generally prevents the policy from taking effect, while the failure to pay subsequent premiums gives the company the right to declare a forfeiture of the policy. What is said in regard to premiums after the first premium relates especially to life insurance. In property insurance the first premium generally covers the insurance for the whole period, either perpetual or for a term of years, as the case may be. In life insurance the premiums are payable at certain periods during the term of the policy. It is important for a person paying the premiums on a life policy to be careful

to pay before the last day for payment expires. Frequently, after a life policy is issued, the company finds out something which makes it desire to forfeit the policy. The insured may, after the issuance of the policy, contract some fatal disease, and in this case some few companies are constantly on the alert to take advantage of the non-payment of a premium when it falls due.

(A) *Who has an insurable interest.*

A man has an insurable interest in his own life to any amount he chooses to pay premiums upon. Certain relatives have a right to insure each other's lives, although they may have no pecuniary interest in each other.

A husband may insure the life of his wife and she may insure his life. A son has an insurable interest in the life of his father or mother. One who is treated as a son or daughter of another, who is not a blood relative, generally has an insurable interest in such other's life. A sister who is supported by her brother may take out insurance on his life. One has no insurable interest in the life of his mother-in-law or of his father-in-law or his uncle or aunt or cousin. A creditor may insure his debtor's life. A brother who supports his sister, under circumstances tending to make her his debtor, has an insurable interest in her life. A surety on an official bond has an insurable interest in the life of the obligor. Generally, it may be stated that, where one is not very closely related to another, he has no insurable interest in the other's life, unless he has some pecuniary interest. If a man insures his own life, and pays the premiums, he may name as beneficiary one who has no insurable interest in his life. The case is different, however, where the assignee of the policy, or the beneficiary, pays the premiums. In such case he must have an insurable interest. See *Harvey's Estate* (1906), 15 D. R. 298.

One who has no insurable interest, but who pays the premiums, is not entitled to the proceeds of the policy. Where a beneficiary having an insurable interest in the life of another assigns the policy to one who has no interest, the assignee who pays premiums and gets the money from the company must

pay it over to the party who has transferred the policy to him, less any premiums paid by him.

The act of June 5, 1883, providing for the incorporation of mutual assessment companies for the insurance of life, provides that when a policy or certificate is issued by such company, and the premiums are paid by another person than the one insured, there must be an insurable interest; and such policy or certificate shall be invalid "when the beneficiary or assignee thereof is solely and only interested in the death of the insured."

The courts will not allow a wagering contract upon the life of another. A creditor may insure his debtor's life for a greater sum than the debt, and interest thereon during the expectancy of the life of the debtor. In order, however, to prevent speculation on the debtor's life, it is said that a creditor will not be allowed to recover on a policy upon his debtor's life, in an amount wholly disproportionate to the amount of his debt. He may take out a policy for an amount which will give him reasonable protection under the circumstances, but the amount of the policy must not be so greatly in excess of the debt that it is clear he is wagering upon his debtor's life.

The expectancy of life is determined by the Carlisle tables or the American tables, which have been prepared by the insurance companies. These tables are based upon the probable length of life of a healthy person, and give a practical way of determining how long a person of a given age will probably continue to live.

(B) Beneficiaries.

Where one takes out a policy on his own life, and designates another to receive payment from the company upon the death of the insured, the beneficiary has an irrevocable interest, if the insured has not reserved the right to revoke. If the insured makes a default or does any act which avoids the policy, the beneficiary cannot recover from the company. In order to give the beneficiary the interest above stated it is not necessary to deliver the policy to him. In some mutual companies the rules permit the members to change the beneficiaries.

The act of April 15, 1868, provides that a person may take out a policy on his own life, for his wife's benefit, and she may recover the money irrespective of claims of creditors of the insured. In such case, the wife being named in the policy as beneficiary, the question of fraud upon the creditors of the insured cannot be brought up. Where, however, a man *assigns* to his wife a policy on his own life at a time when he is indebted, she must show that he was solvent, although the wording of the act might raise a doubt on this point. She must overcome the supposition that the assignment to her was made in fraud of his creditors. This act protects not only the wife, but also the children and other dependent relatives.

When a man takes out a policy on his own life, but it is agreed that it shall be payable directly to a third person who is named as beneficiary, the latter takes a vested interest in the policy. It passes to his estate although he dies before the insured. If the insured reserves the right to change the beneficiary, and the beneficiary dies, and the insured dies without having made any change, the estate of the beneficiary is entitled to the insurance money.

Frequently a policy provides that it shall be void unless payment of the premium is made to an agent of the company having written authority to receive payment. Nevertheless, if a company appoints an agent without written authority to deliver the policy and collect the premium, the receipt of the premium by the agent binds the company. In such case the company has waived the said condition of the policy. Where there is such a condition the company may waive it by its course of dealing with its agent. Often the company accepts the personal liability of its agent for the premium, and binds itself, although the premium may not have been actually paid. Where there is such an arrangement the company is liable on the policy, although payment of the premium is not made to the agent until after a loss has occurred. See, however, *Marland v. Royal Ins. Co.* (1872), 71 Pa. 393; *Murphy v. Ins. Co.* (1906), 30 Super. 560.

Besides the condition that the policy shall not become binding until the first premium is paid, policies sometimes provide that no agent may without written authority waive any

of its conditions. In such case, where the policy remains undelivered, and the premiums unpaid at the time of the loss, the insured cannot recover merely because the agent notified him that a policy had been issued, although the agent was authorized to deliver policies on payment of premiums.

(C) *Reality of consent.*

The act of June 23, 1885, provides that "whenever the application for a policy of life insurance contains a clause of warranty of the truth of the answers therein contained, no misrepresentation or untrue statement in such application, made in good faith by the applicant, shall effect a forfeiture or be a ground of defense in any suit upon any policy of insurance issued upon the faith of such application, unless such misrepresentation or untrue statement relates to some matter material to the risk." Where the matter stated and warranted to be true is material to the risk the policy is avoided if the matter was false. In such case, the question of good faith is not material. Every fact is material which increases the risk and which would entitle the company to ask a higher premium if they had knowledge of it. The act of 1885 was passed for the benefit of the insured, and he cannot waive the benefit of it, even though the policy makes a provision which is intended to relieve the company from the operation of the act.

If the insured makes a false representation of a material fact, that avoids the policy, although death did not result from a cause connected with the matter which was misrepresented. For instance, where the insured says in his application that he has never been attended for any serious disease, and he afterwards dies from an injury received in an accident, it is a good defense to a suit on the policy to prove that he had been treated for some serious disease prior to the time he applied for the insurance. See *Rinker v. Ins. Co.* (1906), 214 Pa. 608.

The act of June 10, 1881, makes it a misdemeanor punishable by fine or imprisonment, or both, to obtain a life policy by means of false representations made knowingly. See also the act of May 11, 1881, referred to in Chapter LIII, subdivision (B). *Fidelity Co. v. Ins. Co.* (1906), 213 Pa.

(D) Suicide; execution for crime.

The risk in a life insurance policy is the death of the insured, but the policy does not cover every death. What is meant is death in the usual and ordinary course of events, that is to say, death by ordinary casualty. Generally the policy provides that it does not cover death at the hands of the government. Thus, if a criminal is sentenced to death and is hung, his estate cannot recover upon a policy of insurance upon his life. Ordinarily the policy provides that it will not cover death by suicide, whether the suicide occurs when the insured is sane or insane. This provision generally contains a time limit, say of two years from the time the policy was issued. If the policy says nothing about suicide, and is payable to another person who has an insurable interest, suicide will not avoid the policy. The rule is otherwise where the policy is payable to the estate of the insured. In this, as in all other matters pertaining to insurance, one should study the terms of each particular policy, for they may decide the question at issue.

(E) Statutory regulation of insurance companies and agents.

Insurance companies are largely governed by acts which deal specially with the insurance business. See the following acts: April 4, 1873; May 1, 1876; June 5, 1883; June 23, 1885; April 26, 1887; May 10, 1893; May 23, 1895; July 9, 1897; May 8, 1899; and June 10, 1901. In these acts one will be able to trace the development of the present system of state regulation of domestic and foreign insurance companies.

The case of *Bartlett v. Rothschild* (1906), 214 Pa. 421, shows what heavy liability is incurred by agents of foreign insurance companies which do business in Pennsylvania without authority. Under the act of May 1, 1876, sec. 48, an agent of a foreign insurance company which does not comply with the laws of Pennsylvania, is personally liable on all contracts made by or through him on behalf of any such company; and it is immaterial that the contract of insurance was not made in this state. Other penalties are also prescribed.

BOOK FIFTH

THE ESTATES OF DECEDENTS

PART I

THE MANAGEMENT OF DECEDENTS' ESTATES

CHAPTER LVI.

THE GRANTING OF AUTHORITY TO ADMINISTRATORS AND EXECUTORS AND THE REVOCATION THEREOF.

In the present book we shall study the duties of those who take charge of decedents' estates from the time when they first qualify until they file their final accounts. Where a person is appointed by will to take charge of a decedent's estate, he is called an executor. Where he is appointed by the Register of Wills, he is called an administrator. The executor's duties which we shall consider one by one may be enumerated as follows: (1) To prove the will; (2) to qualify as executor; (3) to give public notice of his appointment; (4) to file an inventory and appraisement; (5) to collect what belongs to the estate; (6) to pay the decedent's debts and the costs of administering the estate; (7) to pay the collateral inheritance tax and other taxes in proper cases; (8) to file his account; (9) to have his account audited; (10) to have the adjudication upon his account confirmed; (11) to pay over whatever is awarded by the adjudication; (12) to file orders for the satisfaction of such awards, and obtain his discharge. An administrator's duties are the same as those of

an executor, except that in cases where the decedent has left no will, the administrator need not perform the first duty mentioned in the foregoing list, that of proving the will.

The steps mentioned in the preceding paragraph should usually be followed in the settlement of decedents' estates. In the majority of cases, however, some of them are neglected. Sometimes the relatives of a decedent dispense with all formalities, and divide the effects as they may think best. This should never be done where the decedent has left a will, for those who meddle with his estate may get into trouble. When a man dies without leaving a will, and there are no creditors, it is sometimes proper for the relatives to divide up his estate without having an administrator appointed. This should not be done where any of those entitled to share in the estate are not of full age and sound mind. Neglect of legal formalities in dealing with minors or lunatics is likely to lead to future misunderstandings. Even though the decedent has left no will, and all his relatives that are entitled to share in his property have full contractual capacity, they cannot dispense with the observance of formalities if the rights of creditors may be injuriously affected. Suppose that a man dies without making a will, and that the only relatives interested in his estate are two daughters. Suppose they parcel out his effects between themselves, one of them taking a claim against a certain debtor of the decedent. The debtor should refuse to pay the debt to her unless she can give the clearest proof that the estate is not indebted to anybody, and that she alone is entitled to receive payment. If the debtor pays her, and it turns out later that the estate is in debt, an administrator may be appointed who can make the debtor pay the money over again. In case you owe money to a decedent's estate, you run a great risk if you pay it to anyone but a regularly appointed representative, authorized by law to take charge of the decedent's affairs.

Needless to say, a creditor of the decedent need not be particular as to who pays him, for if any of the relatives of the decedent choose to do so, their money is as good as that of the executor or administrator. If a creditor is not paid,

however, he has a right to demand that letters of administration be taken out, and someone appointed to look after the estate. The creditor who is once paid cannot meddle with the estate, but he has a right, so long as he remains unpaid, to insist that his interests be safeguarded.

Just as it is dangerous to pay debts to anyone but the representative of the decedent's estate, so it is dangerous to pay money for property forming part of the estate to any relative who assumes to be taking charge of the estate without proper warrant and authority from the Register of Wills. In the case of *Roumfort v. McAlarney* (1876), 82 Pa. 193, it appeared that two men had been law partners. One of the lawyers died, and his library remained in the office in the possession of the survivor, McAlarney. The deceased partner's widow undertook to settle his estate without taking out letters of administration, and made a sale of the library to McAlarney. The latter never paid for the books, although that would not have prevented the passage of title to him if the widow had possessed the authority to represent the estate in making the sale. Afterwards a third party took out letters of administration on the deceased lawyer's estate, and brought an action of replevin against McAlarney to recover the books. The court held that he could get them back, for no title had passed by means of the widow's sale. It would appear that if the widow had enjoyed possession of the library, and had sold it to McAlarney, received the money, and *applied the money received to the payment of the decedent's debts*, there would have been a sort of administration, not precisely legal, but accomplishing the purposes of a legal administration, which the courts would have been loath to disturb. As it was, however, the Supreme Court reached the conclusion that no title had passed by virtue of the widow's attempt to make a sale of the library.

It is plain, then, that if anyone dies, leaving personal property in any considerable amount, an executor or administrator should be duly qualified by the Register of Wills to manage his estate, especially if there are bills to be paid by the estate or collectible claims to be enforced against debtors of the estate.

An executor is named by the decedent himself to execute his will. An administrator is appointed by the Register of Wills to administer the affairs of the deceased, where the deceased has not appointed any executor, or the executor appointed does not qualify. If the will does not name an executor, or the executor named has died, or is unable or unwilling to act, then an administrator must be appointed. Such an administrator is an administrator *c. t. a.*, that is, an administrator *cum testamento annexo*. The words "*cum testamento annexo*" are Latin words meaning "with the will annexed." Such an administrator is different from the ordinary administrator, in that his duties may be marked out by the terms of the will, while the ordinary administrator has no will to guide him, but only the general law on the subject of the administration of decedents' estates. Suppose an estate has been partially wound up by an administrator who dies or is removed before he has fulfilled all his duties. It becomes necessary then to appoint a successor, and this successor is called an administrator *d. b. n.*, that is, an administrator *de bonis non*. These Latin words indicate that the administrator is to take charge of the affairs not already settled by the first administrator. Finally, let us suppose that an executor has died or been removed before the estate is wound up, and it is found necessary to appoint a successor. This administrator is called an administrator *d. b. n. c. t. a.* These six initials which form part of his title are easily understood by putting together what has been said already. The administrator *d. b. n. c. t. a.* is to be guided by the will, and is to finish the work left incomplete by the executor.

Sometimes the Register of Wills appoints an ancillary administrator. The word "ancillary" comes from the Latin word "ancilla," meaning a handmaid. An ancillary administrator is a subordinate to some foreign executor or administrator. As we shall see a little later, the State of Pennsylvania does not fully recognize executors and administrators appointed in other states or countries. In order that such foreign representatives may have suit brought or attend to certain other duties in this state, it is generally necessary

that somebody qualify here. This enables the Pennsylvania creditors of the decedent to get the benefit of the funds which are collected here by the ancillary administrator. It would be unwise for this state to let a foreigner come here with all the rights and privileges of a domestic administrator, collect all the debts due in Pennsylvania to the deceased, and then distribute the estate, say, out in California, so far off that it might be impracticable for Pennsylvania creditors to look after their interests. It is only fair that a foreign executor who wants to get the aid of our laws in collecting claims from debtors located in this state should qualify here, and take care of local creditors of the estate. An ancillary administrator is, therefore, an administrator supplemental and auxiliary to some general administrator or executor appointed outside of Pennsylvania. Sometimes a Pennsylvanian is appointed ancillary administrator in this state, and sometimes the foreign executor comes here and receives a second appointment as ancillary administrator in Pennsylvania. The funds collected here by the ancillary administrator must be kept in his possession as separate funds. Pennsylvania creditors have a right to look to these funds for payment of their claims, and a creditor from outside has no right to come into Pennsylvania in order to get a dividend out of the assets in this jurisdiction. The ancillary administrator accounts in the same way as the ordinary administrator or executor, and if a balance remains in his hands after he has wound up all the decedent's Pennsylvania affairs, this balance must be remitted to the principal executor or administrator in the foreign state. The courts are not bound to order the ancillary administrator to remit the balance to the foreign state, for if there are special circumstances inclining them to have the balance distributed here, they may adopt that course.

The act of March 31, 1905, provides that executors and administrators in this commonwealth shall not be required to deliver to any foreign executor or administrator any fund which has been devised or bequeathed, in whole or in part, by will of the decedent, valid under the laws of this commonwealth, and duly probated at the domicile of such decedent,

where any person claiming such fund, or any part thereof, is a citizen of this commonwealth. But such fund shall be distributed, under the direction of the Orphans' Court of the proper county, to legatees, devisees and creditors, according to the terms of said will and the laws of this commonwealth.

The act of March 15, 1832, directs that no appointment of an executor or administrator made outside of this commonwealth shall confer any of the powers and authorities possessed by an executor or administrator under appointment within this state. The act of April 14, 1835, and later acts, however, give a foreign executor or administrator power to sell and transfer any State of Pennsylvania bonds standing in the name of the deceased, and to transfer the stocks and bonds of any municipal or private Pennsylvania corporation that have been left as part of the estate. As a general rule, the foreign executor or administrator cannot sue to recover assets in this state, and for that purpose, an ancillary administrator is essential. A debtor who lives in Pennsylvania, however, is at liberty to pay his debts to a foreign executor (so long as no local creditor objects), and the foreign executor's receipt will protect him.

What is an *administrator pendente lite*? The words "pendente lite" mean "pending litigation," that is, during a lawsuit. Very often there is a great deal of trouble after a man dies as to the validity of a disputed will, or as to the rights of contending parties to take charge of the estate. Such disputes are often kept up for months, and meantime the estate needs somebody to watch over it. The temporary administrator who is appointed to take charge pending the settlement of the dispute is called an *administrator pendente lite*. He goes ahead to wind up the estate, but as soon as it is found which of the disputants is in the right, a regular executor or administrator is qualified and the *administrator pendente lite* steps out. He must account for what he has received, and the balance found due by him is awarded to the regular administrator or executor when appointed. The Register of Wills usually tries to choose as an *administrator pendente lite* some person who is not strongly allied with

any of the contending factions. A large range of discretion is given to the Register of Wills in making this choice, but he should usually appoint some near relative of the decedent.

What is an executor *de son tort*? The translation of the French words is "of his own wrong." A person who wrongfully intermeddles with the estate of a decedent, and presumptuously takes it on himself to run things is called an executor *de son tort*. Since he has assumed to be an executor, he is liable, of course, to the rightful executor or administrator for whatever property has come into his hands. The executor *de son tort* cannot, however, be ordered to account before the court, because he does not figure as a real officer of the court in settling up an estate, but only as an intruder who has wrongfully taken charge of certain property. The executor *de son tort* is entitled to credit, however, for legal debts of the decedent paid by him. Of course he has no right to commissions, for he has thrust himself officiously into the place of a regular executor.

The next question to be treated regards the appointment of executors and administrators. In the case of a will, it is plain enough that the naming of the executor is done by the decedent who has made the will. In the case of an administrator, where there is no executor, the act of March 15, 1832, provides that the Register of Wills of the county where the decedent has made his home shall appoint an administrator. He grants letters of administration to the widow, if any, of the decedent. If the decedent leaves no widow, or if she is unable or unwilling to act, the Register appoints such of the relations as by law may be entitled to the residue of the personal estate, or a share thereof, after payment of the debts. The person who is going to get for himself all the surplus after payment of debts can usually be depended upon to look out sharply for the welfare of the estate. The order of preference which, in accordance with the act of 1832, usually governs a Register in deciding who may be entitled to letters, is as follows: First, the widower or widow of the deceased. Second, children. Third, grandchildren and other lineal descendants. Fourth, father or mother. Fifth,

brothers and sisters. Sixth, descendants of brothers and sisters. Seventh, grandfather or grandmother. Eighth, uncles or aunts. Ninth, cousins. Tenth, other descendants of grandfather or grandmother. Eleventh, distant relatives. Numerous reasons may dispose the Register of Wills to depart from this order of preference in a particular case. He will never grant letters of administration to a minor, or to a person of full age who is not of sound mind or who is an habitual drunkard or who is insolvent or in jail. A minor who would be clearly entitled to the appointment, but for his age, sometimes has another person appointed temporarily, and qualifies himself after reaching twenty-one. It is not proper to appoint one who stands in a hostile position to the estate. Where two persons are in the same rank of preference, the fact that one is older than the other may incline the Register to choose him, although he may, on the contrary, prefer the younger for good reasons. Again, where a man and a woman bear the same relationship to the decedent, the man is preferred to the woman. The Register may, if he chooses, select more than one administrator out of the class entitled, but he is not bound to appoint all the members of that class. For instance, there may be no nearer relative than first cousins. It is not necessary for the Register to appoint all the first cousins to take charge of the estate together. Ordinarily only one administrator is appointed. In case all the relatives refuse or are incompetent, the Register must appoint either one or all of the principal creditors of the decedent who may apply for appointment, or else any suitable person, at his discretion.

The act of 1832 provides that the Register may join with the widow such relation or relations as he shall consider best fitted to administer the estate, preferring always of those so entitled such as are in the nearest degree of blood relationship with the decedent, and also preferring males to females. Many widows need assistance in such matters. The act provides further that the husband shall be entitled to preference above all other persons, if the decedent was a married woman. If the decedent was a married man, the widow is not exclusively

entitled, for the Register may, if he deems fit, associate with the widow such near relatives as the act mentions.

The act of 1832 provides also that in the case of the appointment of an administrator *c. t. a.*, where the will annexed has given the residue of the estate to one or more persons, such person or persons shall have the right to act as administrator *c. t. a.*, but the Register may select a single one to act if there are a number of people interested in the residue of the estate. The entire law on this subject seems to be framed in order to give the right to administer the estate to those who are best entitled by reason of their relationship and their interest in the estate itself, subject to variations for good cause.

When an administrator is appointed by the Register of Wills, the latter gives him letters of administration. These letters are the warrant of authority upon which the administrator acts. They consist of a document under the Register's official seal setting forth the appointment. In like manner, where an executor is appointed by a will, and the will is proved at the Register's office, letters testamentary are given to the executor, as a token of his authority to take charge of the estate and of the due probate of the will. A person who wants to qualify as an executor or administrator goes to the office of the Register of Wills with a sworn petition setting forth the death of the decedent, and the time and place when it occurred. It states also that the decedent had his home in the county where the office of the Register of Wills to whom application is being made is located, because the letters should be granted in the county of the decedent's residence. Sometimes Pennsylvanians die outside of the state, for a great many go to the seashore and to various distant health resorts in times of sickness, but the occurrence of death in a foreign state does not prevent the granting of letters by the Register of the county where the decedent had his domicile. The question as to the real home of the decedent is often perplexing. Some people lead a roving life, and it is hard to say just where they make their home. Their intention in this respect is important. Thus, if a Philadelphian lives

most of the year in New York, but always regards Philadelphia as his home, he remains a Philadelphian, and the Register of Wills of that county will grant letters of administration on his estate. Before an executor can receive letters testamentary, the will from which he derives his appointment must be duly proved. The probate of wills is to be treated in the second part of this book. Aside from proving the will, usually the only thing to be done by an executor in order to qualify is to prepare a petition. This petition sets forth the same facts as the administrator's petition described below, except that it need not mention anything about the decedent's widow or husband, heirs and next of kin.

When a petition for letters of administration is presented to the Register of Wills, it must state the residence of the decedent, the time and place of his death, and the names and residences of the decedent's widow or husband, heirs and next of kin. It must state also the value of the decedent's personal property and of his real estate (less incumbrances) as nearly as can be ascertained, and where the real estate is located. This petition is sworn to, and if the person who applies for letters of administration seems to be entitled to them, the Register makes the appointment at once, after getting his fees, which are scaled according to the size of the estate. If there is a contest as to who shall be given letters of administration, the register hears the evidence and decides the matter subject to an appeal which may be taken by the defeated party to the Orphans' Court.

In some cases the nearest relatives of the deceased feel averse to undertaking the work of settling up the estate. The practice is to have the nearest relatives who want to pass over their rights to somebody else, sign a renunciation. Of course, if they once renounce they cannot have a substitute appointed and then arbitrarily remove the substitute and have themselves appointed instead. If they entirely renounce, their rights are ended. On the other hand, if they once qualify, and take charge of the estate, they are bound to go ahead with the performance of their duties and to account for what they have received and paid out. It may be men-

tioned that sometimes a man making his will appoints the same person executor and also trustee under one will. As executor this person's duty is to collect assets, pay debts, and wind up the estate. As trustee, he is bound to take charge of some particular estate created by the will, and manage it, perhaps for a long period of years. The duties of executors and trustees are so different, that where the same person is appointed to both positions by a will, he may renounce his right to become trustee, while asserting his right to act as executor.

Most executors do not have to give bonds, except under certain special circumstances, because the appointment of them in the will indicates that the maker of the will reposed personal confidence in them. It is quite different in the case of an administrator, because the Register of Wills cannot tell whether the nearest relative of the decedent is responsible financially, honest and capable, or the very reverse. Accordingly, the act of 1832, which is the foundation of the Pennsylvania law of decedents' estates, provides that the applicant for letters of administration must give a bond with two or more sufficient sureties. This bond is usually for an amount double the estimated value of the personal property of the deceased. Inasmuch as the administrator cannot meddle with the real estate, except upon special order from the Orphans' Court, it is not necessary to consider the value of the decedent's real estate in fixing the amount of the bond. At least one of the sureties should own realty, and this realty should be valuable enough to protect the estate against any loss.

Where an executor or trustee is believed to be experienced and honest and where he will be able to wind up the estate in a year, there is seldom any use in drawing up the will so as to make him give a bond. Where the term of office of an executor or trustee is likely to last for many years, the person who appoints him should in many cases provide that a corporate bond must be furnished to guarantee his fidelity. Unless the person who makes the will directs this to be done, he is considered to repose full personal confidence in his executor or trustee, and the latter is not usually required to furnish a

bond. On the other hand, no such notion prevails in the case of an administrator's appointment, for an administrator is not chosen by the decedent, but is usually chosen because of his relationship to the decedent. The act of March 15, 1832, directs that if any Register shall grant letters testamentary to an executor who is not an inhabitant of Pennsylvania, or letters of administration to any person or persons whatsoever, without having taken a bond and sureties, such letters shall be void and every person acting under them shall be treated as an executor *de son tort*. The act makes the Register liable to pay all damages which shall befall any person by reason of the Register's failure to require the bond with sureties. An executor who is not an inhabitant of Pennsylvania is not so easily sued, and brought under the control of our courts as one who lives here, and, therefore, a foreign executor must furnish a bond with sureties, even though the will is made by a citizen of Pennsylvania, and the estate is wound up here.

Where the provision that the administrator must give a properly secured bond is disobeyed, the letters of administration are void. The letters of administration are also void if the Register grants them more than twenty-one years from the date of the death of the decedent, unless the Orphans' Court has ordered this to be done for some special reason. When twenty-one years have elapsed from the date of a man's death without the taking out of any letters, it is presumed that all the decedent's affairs have been settled, and the courts dislike to disturb matters after such a lapse of time.

Another case in which letters of administration are void is where a will is unexpectedly found after letters of administration have been issued by the Register. Where an administrator has been appointed on the supposition that no will exists, and later a will turns up, it would be wrong to make the administrator suffer any loss on account of acts which he has done in good faith. Accordingly, the statute of February 24, 1834, directs that all the administrator's acts that have been done in due course of law, and without notice of a will, shall not be impeached or set aside in spite of the subsequent finding of the will. The administrator must at once

step out in favor of the executor who has been appointed by the will.

What power has the Register to revoke letters which he has granted? If he has had a number of applicants for letters of administration, and has chosen a certain administrator out of several who were in the same degree of relationship to the decedent, he has exercised his discretion in making the selection, and he cannot afterwards arbitrarily change his mind, and select another relative who has no better right to the office than the one originally appointed. If a person who is interested in a decedent's estate thinks that an improper choice of administrator has been made, he should apply to the Register to have the letters revoked, and may appeal from the Register's decision to the Orphans' Court. The application to revoke the letters must not be made in the first place to the Orphans' Court, for the Register has primary and original jurisdiction over the matter. In the case of *Comfort's Estate* (1893), 12 Pa. C. C. 571, a Register was asked to revoke letters on the ground that they had been applied for with unseemly haste on the same day that the decedent died. It was held that although such hurried proceedings were scandalous, this fact alone would not be sufficient to justify a revocation. The person who demands that letters be revoked should be one who is interested in the estate. A relative who lives outside of this state has not as good a standing as a Pennsylvanian to object to the grant of letters and to petition that they be revoked. A Register should not usually appoint a foreigner administrator, and, therefore, a foreigner should not have much to say on the subject. Nevertheless, a foreigner's wishes are often respected at the time of the administrator's original appointment if he is largely interested in the estate.

If letters have been revoked, the executor or administrator, whose authority is thus shorn away, should at once prepare an account, if there is anything to account for. This account must be filed with the Register of Wills, and audited in the same manner as ordinary accounts.

CHAPTER LVII.¹THE DUTIES OF EXECUTORS AND ADMINISTRATORS AFTER THEY
HAVE QUALIFIED.

After an administrator or an executor has been appointed, and has fully qualified, notice of his appointment must be advertised in one newspaper published at or near the place where the decedent resided, once a week during at least six successive weeks. This notice should give the names and addresses of the executors or administrators, although in many cases where an administrator may want to refer matters directly to his attorney, the latter's address is the only one published. The rules of court of some counties require additional advertising. The act of April 30, 1901, requires also that the same kind of notice shall be published in a German daily newspaper of general circulation printed in the county where the decedent died, provided there are over forty thousand emigrants from Germany in the county. This act is disregarded in many cases. The publication of notice is to inform creditors of the death of their debtor, so that they may present their claims promptly and to the right persons. The act of February 24, 1834, directs that when property is left to any public corporate body by any last will and testament, the executors shall within six months after they receive letters inform the corporate body of the gift. The executors must also state their names and addresses to the corporate body in question.

(A) Inventory and appraisement.

The act of 1832 makes it the duty of the executor or administrator to file a true and perfect inventory of all the goods, chattels and credits of the deceased, so far as they can be ascertained, in the register's office, within thirty days from the grant of letters. The act provides that in the case of the will of a decedent proved in another state or in a foreign country upon which ancillary letters are taken out in Pennsylvania, the inventory shall cover only the goods,

chattels and credits of the decedent within this commonwealth. If an inventory is filed, and the executor or administrator learns subsequently of other assets belonging to the estate, he should make an inventory of them, and file it within four months from the time he discovers them. The inventory should include all bonds, notes and other evidences of debt due to the decedent, as well as all other claims and demands for money, and all kinds of personal property owned by the decedent at the time of his death. If the executor himself owes the decedent any money he should include his own debt in the inventory.

The document filed in court is more than a mere list of the assets, for the act of 1832 requires the executor or administrator to have two appraisers put a value on the various items which appear in the inventory. These appraisers must be sworn or affirmed to appraise the assets well and truly, and without prejudice or partiality. The inventory and appraisement, as the paper filed is called, must be recorded by the Register of Wills. Many executors or administrators neglect to file an inventory or appraisement. Usually the Orphans' Court, when the account is finally audited, does not object to the failure to do this. The act does not name any punishment for disobedience to this provision, but any person interested in the estate may have a citation issued after the lapse of thirty days from the granting of letters to compel the inventory and appraisement to be made up and filed. It is a good answer to the citation if the executor or administrator swears that no property has come into his hands, and that he has not learned of the existence of any assets. As a general rule only the items of personal property figure in the inventory, because the executor or administrator usually has nothing to do with real estate. It is best to have the inventory made as complete and detailed as possible, but considerable latitude is allowed to the discretion of the appraisers. If a man dies leaving only a small shoe-mending shop, the inventory of his effects would naturally go into more minute particulars than in the case of a man who leaves a number of shoe factories and shoe stores.

The Register is the proper person to whom application should be made for the issuance of a citation to compel the executor or administrator to file an inventory and appraisal. If the inventory and appraisal are not correct, the executor or administrator may have it amended afterwards. Nobody interested in the estate need accept it as absolutely binding and correct. If, for instance, certain property is valued at an absurdly low figure, and is turned over to a friend of the executor at that figure, the other parties interested in the estate may impeach the transaction. An executor should be careful not to have the effects of the deceased appraised too high, for this raises the expectations of the persons who are interested in the estate. They are apt to blame the executor if the prices realized by him at a sale of the assets fall much below the appraised values. Usually, however, he cannot be surcharged with the difference between the appraisal and the selling price of the goods if he has had such goods sold at public auction.

As a general rule, all the property of the decedent, if it is to be sold, should be sold at public auction. This protects the executor, but he is not protected if he sells privately, unless he is prepared to show that what he does is for the best interests of the estate. It sometimes happens that family pictures and articles which may have a sentimental value in the eyes of a few persons can be disposed of to better advantage at private sale, and the executor will not be surcharged if he adopts a course which benefits the estate. He takes a great risk, however, if he disposes of valuable property at private sale without at least notifying all the parties in interest. He should not sell any assets to himself, for we saw in the chapters on Agency that an agent must not put himself in a position where there is a conflict between his duty as agent and his natural desire to buy property for himself at the lowest possible price. Occasionally there may be special reasons for permitting an executor or administrator to buy property belonging to the estate, but he should always protect himself by petitioning the Orphans' Court for permission to purchase in his own right.

At the beginning of the previous chapter, twelve steps were enumerated, leading an executor from the probate of the will down to the conclusion of his work. The same steps, except the first, are taken by an administrator in winding up an estate. An executor and an administrator have very much the same duties, and when we speak of one of them, it must ordinarily be understood that the remarks apply to the other also. We come now to the subject of an executor's or administrator's control over the property left by the decedent. Ordinarily they have full powers over the personal property. An administrator, however, usually has nothing to do with realty; neither has an executor, unless the will so provides.

(B) *Powers and duties of executors and administrators.*

The distinction between the executor's duties as to *realty* and his duties as to *personalty* is seen in the two following cases. In the case of *Burton's Estate* (1894), 3 D. R. 755, it appeared that Burton's executor had set apart \$7,000 out of the personal estate to secure the payment, when due, of a mortgage, with its accompanying bond. The bond and mortgage had been executed by Burton, and were secured upon real estate owned by him at the date of his death. The executor had paid interest thereon accruing after Burton's death. The court held that although it was a lien on Burton's realty, yet it was his own personal obligation, and payable out of any funds in his executor's hands. See *Tubb's Appeal* (1894), 161 Pa. 252, and *Graff & Co.'s Estate* (1891), 139 Pa. 69. In *Hirst's Appeal* (1880), 92 Pa. 491, the mortgage on which Hirst's executrix had paid interest was a lien upon a house and lot owned by Hirst at the time of his death. Hirst, however, had not signed either the mortgage or the bond accompanying it, having bought the house and lot subject to the mortgage. It was not his personal obligation, but only a lien on his realty. His executrix, therefore, was not allowed credit in her account for payments of mortgage interest.

In the case of most estates the executor or administrator is able to pay the debts and funeral expenses, and settle up matters, without touching the realty. The realty usually goes to the nearest relatives, in case there is no will, and to the persons to whom it is left, in case there is a will. The personal property is to be used for payment of debts and funeral expenses, and usually the realty is not touched for these purposes, unless there is a deficiency after applying all the personal property to the payment of debts. In case of such a deficiency, a petition should be made within two years, requesting permission from the Orphans' Court to sell the real estate, or a portion of it, for the payment of the remaining debts.

The sale under order of the Orphans' Court for the payment of debts should be made within two years from the decedent's death, because the real estate ceases to be liable for the payment of debts after two years, unless there is a provision to the contrary in the will. If the will contains no provision extending the lien of debts beyond two years, a creditor who is not paid, and who has not recovered judgment upon his claim, should learn whether or not the debtor left real estate. If there is any realty, the creditor should do one of two things: first, try to persuade the executor or administrator to file a petition for permission to sell the realty for the payment of debts; or, second, bring suit upon his own individual claim. If the creditor does not have the judicial sale made or start his own suit within two years, his lien on the real estate is lost forever. The advantage of a creditor's bringing a separate suit against the estate is that if no such sale of real estate for the payment of debts is made within the period mentioned, the creditors who are vigilant in asserting their rights may gain an advantage over those who have failed to bring suit on time. A recent act of the Pennsylvania legislature requires the creditor's suit against the estate to be indexed in the judgment index of the county where it is brought. In the case of a bond or other debt, which will not become payable within two years after the decedent's death, a copy of the bond or a detailed

statement of the claim should be filed during the two years with the prothonotary of the county where the real estate to be subjected to the lien is situated. Act June 14, 1901.

An executor should not collect rents, unless he has been authorized by the will to take charge of the decedent's realty. He should, however, collect arrears of rent which have fallen due in the decedent's lifetime. Such arrears are considered as a personal debt of the tenant, and not as current income from real estate. If a will merely gives an executor power to sell real estate, he has no authority to take charge of it. If, however, the will orders him to sell it, it is usually implied that he shall manage it until the sale takes place. He should, as soon as appointed, proceed to gather in all the personal property belonging to the estate. This includes money due on life insurance policies which are made out in favor of the decedent or of the decedent's estate. If any insurance policy is payable to the decedent's widow or children, the executor has no right to the proceeds, for such policies belong to the beneficiaries.

If the decedent has been in business for himself, the executor should as a rule close it out as soon as possible. A delay in doing this, however, may be justified if the executor finds it necessary to run the business for awhile in order to save heavy loss incident to a sudden closing out. As we saw in the discussion of partnership, the executor of a deceased partner has nothing to do with the partnership effects, for the right to liquidate belongs to the surviving partner.

The executor often finds that the decedent has a bank account, and, perhaps, shares of stock and registered bonds of various corporations. The executor will be asked for proof of his authority when he attempts to collect the money in bank or to transfer the stocks and bonds. This proof is supplied by documents called "*short certificates*," which may be procured of the Register of Wills, usually for fifty cents apiece. One of these short certificates, which sets forth briefly the fact that the executor has charge of the estate in question, is left with each company that transfers stocks or bonds standing in the decedent's name. The company thus

has a document to show why it transferred the stock or bonds upon the signature of anyone but the decedent himself, in whose name they were issued. The executor's signature coupled with the short certificate protects the company, for he is presumed to have authority to dispose of the decedent's personal property.

If the decedent has become entitled to a share of personal property in another estate before his death, but this share has not been paid to him, the executor has a right to claim it. Suppose X dies, and either by his will or by the intestate laws, his property is to go to Y. Y's rights become complete at the moment when X dies, and if Y dies the following day Y's executor has a right to the entire personal estate left by X.

Suppose a man dies owning, among other property, twenty shares of B. & O. stock, and these twenty shares of stock are left by the terms of his will to his cousin. Has this cousin, the legatee under the terms of the will, or the executor a right to the custody of the stock certificate? The general rule is that the executor is for the time being entitled to the possession of all personal property left by the decedent. The reason is that the executor is a trustee not merely for legatees, but also for creditors. If there were a shortage of assets, the rights of the creditors would be superior to those of the cousin. This rule may be slightly departed from under special circumstances. For instance, in one case it appeared that certain chattels were specifically bequeathed to a son of the decedent, and he was in possession of them at the time. The executor petitioned the Orphans' Court to make the son hand over these goods, alleging that the estate was insolvent. The son asserted that the estate was not insolvent, and stated that if he were compelled to surrender the goods it would seriously hamper his business. The court emphasized the principle that an executor's duties cannot be properly performed unless he is placed in control of the personal property of the decedent. They decided, nevertheless, that under the circumstances it would be a hardship to deprive the son of the articles specifically left to him by his father unless they

were required for the payment of debts. Accordingly the articles were allowed to remain in charge of the son upon his giving the executor a refunding bond with security, so that if the estate should prove insolvent the creditors would be protected.

It was stated that an executor has usually nothing to do with real estate left by the decedent. This should be understood in the light of the technical legal meaning of the term real estate. If the decedent in his lifetime has made a contract to sell certain real estate, but the deed has not finally been executed, it is considered that the decedent has converted the real estate into personalty, and, if the contract is afterwards enforced, the executor will be entitled to the proceeds of the real estate. Again, a tenant's lease of real estate is considered to be personal property, and the executor gets the value of the leasehold. Sometimes it is found that a decedent has secured a long lease on property, and the property has enhanced in value, so that the lease is a valuable asset on account of the low rental. The good will of a business is likewise personal property. Mortgages owned by the decedent pass as personal property to the executor, while, on the contrary, ground-rents do not come into his possession, unless the will so directs, or unless he has to petition to sell them for the payment of debts. The reason for this distinction is that mortgages are personal property, while ground-rents are realty.

Usually an executor or administrator should not undertake to invest the funds coming into his hands. His duty is to wind up the estate. When he converts property into cash he should promptly deposit the cash to the credit of the estate with some responsible bank or trust company. Sometimes, however, where the estate will remain unsettled for years, he should invest money in his hands, in order to make it more productive. A trustee is usually bound to invest funds of the estate, because his duties are of a continuing character. Unlike an executor or administrator, a trustee is usually expected to produce income from the estate in his charge. Indeed, in the case of most trusts, some of the bene-

ficiaries receive no part of the principal of the trust estate, but only income.

The act of 1832 allows a fiduciary to invest funds which are to remain in his possession, and of which he is to distribute the income, but he must invest in United States or State of Pennsylvania bonds, or in Philadelphia bonds, or in first mortgages. Later acts permit investments in bonds of any of the counties, cities, school districts or other municipal corporations in the State of Pennsylvania. Investments may be made in ground-rents, if the Orphans' Court gives special permission to do so. If it becomes the duty of a fiduciary to invest funds, and he has not been given any special authority in the matter, he must confine himself to the classes of securities just mentioned, upon the risk of being surcharged with any resulting loss if he deviates from the rule laid down.

In *Stewart's Appeal* (1885), 110 Pa. 410, a different question presented itself. Stewart, an executor, had *continued to retain* in his possession for a period of four years (pending the settlement of an unusually complicated estate) certain shares of railroad stock which were *not legal investments* within the provisions of the statute. These securities were bringing in dividends, and it did not appear that it was necessary to sell them in order to pay debts. Stewart sold them in 1878, when the market value was quite low. If he had sold them when he first took charge of the estate, or else waited after 1878 for prices to improve, he could have realized much more. The court refused to hold him responsible either for retaining the stock four years or for selling when, as appeared afterwards, the market quotations were at their lowest ebb. All that could be required of him was common skill, common prudence and common caution. The decedent had bought the stock himself, and under all the circumstances Stewart was not to be blamed for failing to sell promptly.

It would be bad for many estates if an executor were always legally bound to dispose of all the stock coming into his hands within one year. Suppose an estate controls the majority of the stock of some small company. It might be impossible

to dispose of this stock within a year except at a great sacrifice, so the courts will not put the executor under the necessity of sacrificing the interests of the estate in order to protect himself. Sometimes a trustee will find that his predecessor has invested in stocks which pay a good dividend. While he would not be safe in buying such stocks in the first place, he may continue to hold them, provided that to do so seems consistent with ordinary prudence. If he can show that careful business men are making such investments with their own funds he can save himself from surcharge, even though the price of the securities which he has retained falls. If debts need to be paid, there is more necessity for selling securities, and for this reason an executor's failure to convert for a long time will be less excusable as against creditors than as against legatees and other beneficiaries. Often beneficiaries are glad to take over securities from an executor, because it saves them the trouble of making an investment if they receive what they are to get already invested.

In *Stewart's Appeal*, stated above, the stock which Stewart held was bringing in a regular income. Where assets do not yield an income there is less reason for holding on to them. Stock in trade and articles in the course of manufacture should be disposed of as quickly as possible, although, of course, the executor should not feel obliged to sell them immediately if to do so would entail a sacrifice. He continues to hold them, however, at some risk. In a Philadelphia case a man who was building a yacht died after having constructed only the hull. Fourteen months afterwards the executor filed an account in which he charged himself with the appraised value of this hull, and asked to have his account credited by the same amount, for he had not yet disposed of the hull. The court surcharged him with the amount on the ground that he should have disposed of the hull, while as a matter of fact he had made no effort to do so.

The executor is a fiduciary, and bound as such to be entirely loyal to his trust, and to observe all the rules laid down by law. At the same time he is not an insurer. He does not warrant that whatever he does will surely redound

to the advantage of the estate. If, for instance, he buys securities in accordance with the law as to legal investments, or in accordance with the provisions of a will which gives him discretion to go outside of legal investments, and shows ordinary prudence in what he does, he is not liable to be surcharged for any resulting loss. He should be prepared to justify any action he may take, and should take receipts, and satisfy himself before paying any claim that it can be legally established in court by proper evidence if it should become necessary to do so.

In *Miller's Appeal* (1858), 30 Pa. 478, a fiduciary was accused of breach of trust. Peter Miller, by his will, left the residue of his estate upon certain trusts, and appointed Samuel Wilhelm trustee to look after the same. Wilhelm was also an executor of the will. He made an agreement with the nephew of Peter Miller, who was Miller's nearest relative, that if the trust as to the residue should be declared invalid, the said residuary estate should be equally divided between the nephew and Wilhelm. The residuary trusts were afterwards declared void and Wilhelm at the settlement of the accounts claimed one-half of the same. The court decided against him.

The policy of the law forbids an executor or trustee to deal with the estate committed to his charge in the manner attempted by Wilhelm. He was not compelled to accept the appointment to the office of executor and trustee, but having accepted the appointment, he was bound to execute it with an eye only to the wishes of the testator as expressed in the will, and the interests of those for whom the testator provided. As trustee Wilhelm was in duty bound to do everything possible to accomplish the purposes of the trust. It was clearly wrong for him to make a contract which would give him a decided interest in defeating the trust. Wilhelm made a bargain with the nephew whose interests were opposed to those which Wilhelm should have protected. This agreement was not enforced, and the nephew was entitled to retain the entire residue.

Frequently the executor or administrator is besieged by creditors, and also by relatives of the decedent who claim as beneficiaries either under the terms of a will or under the intestate laws. It is better to go slow about paying creditors, and there is great danger in paying beneficiaries before the proper time. In the course of a year the executor should know about how the estate stands, and the usual practice is to pay creditors before filing the account, unless it is feared either that the estate may be insolvent or that serious questions may arise when the account is audited as to the validity of the creditors' claims. *Beneficiaries have not the standing of creditors, and come in for a share only after creditors have been paid in full.* In order to prevent the possibility of mistakes which will prove expensive, the executor should ordinarily decline to pay any of the beneficiaries until his account has been filed and the court has ordered distribution. He should usually pay nothing to the distributees who are entitled to the balance after creditors are settled with until ordered to do so by the court. Sometimes the discovery of a new will, or of relatives whose existence was not suspected, may put the executor in a bad position if he has made a premature distribution. If he has distributed in accordance with the court's order he is fully protected, no matter what happens afterwards. Where the beneficiaries are hard pressed for money, the executor may feel disposed to pay small sums to them, if he is sure that it will not cause him any trouble, without waiting until his account is approved, and distribution is ordered by the Orphans' Court. In that case, it is best to get them to sign a refunding bond, which is an agreement to restore the money to the executor, if it is subsequently found that the beneficiary was not entitled to it. A good plan is to have the refunding bond signed by responsible friends of the beneficiary as sureties.

If the executor is afraid that the estate may turn out to be insolvent, he should not pay creditors indiscriminately, because if he pays one unpreferred creditor in full, and there is only enough for a 75 per cent dividend among such creditors, the executor himself will be the loser. If he feels that the

estate will not pay 100 per cent to all creditors, the executor should certainly not pay any of them at once, except such as are preferred by law, but make them wait until the audit. Even though the estate is hopelessly insolvent, perhaps there may be enough assets to justify the executor in paying the preferred claims.

The testator cannot by any direction in his will change *the order of the distribution among creditors*. Their rights are fixed by the act of February 24, 1834, which names this order of preference for the payment of debts: First, funeral expenses, medicine and medical attendance furnished during the last illness of the decedent, and servants' wages not exceeding one year. If there is not enough to pay these claims which are preferred above all others, they all share pro rata in the fund to be distributed. After the payment of all claims in the first rank of preference, rents for a period not exceeding one year must be paid. This preference is restricted to rent accruing before the death of the decedent. Rent which falls due after his death, under the provisions of a lease, may be apportioned, and a preference given to the part which has accrued at the time of the death. If the lessee has agreed to pay certain taxes or insurance as part of the rent, the landlord's claim to compel the estate to enforce the deceased tenant's liability for unpaid taxes or insurance is entitled to a preference. After rents for one year, all other claims for debts against the decedent fall into one class, and are to be paid pro rata, with the exception of debts due the Commonwealth of Pennsylvania, which are to be paid last of all. If one of the preferred claimants has accepted a note from the decedent instead of relying on his unsecured claim, this may put him on the basis of an ordinary creditor, and destroy his preference. *Silver v. Williams* (1828), 17 S. & R. 292.

The necessary costs of administration are to be taken out of the estate before any preferred claimant can get anything out of the general funds of the estate. Few executors would be so foolish as to pay out money required to wind up an insolvent estate if they could not be fully reimbursed.

Those creditors who have secured a valid lien on any part of the decedent's property, may assert their rights as lienholders. Suppose that you hold a first mortgage upon property owned by your debtor, and that he dies. Your mortgage will probably be paid in full, although his unsecured creditors may get very little if his estate is insolvent. Suppose the value of the mortgaged property is sufficient to satisfy only half of your claim. As regards the unpaid half, you may obtain a dividend out of the general funds of the estate, along with the other unsecured creditors. The same principles apply if you have received possession of some of the debtor's personalty, which has been pledged to secure your claim against him.

If you have a lien on real or personal property, you will not be obliged to wait until the expiration of a year before taking advantage of your rights as lienholder. You may, in accordance with the terms of the agreement which gave you security, proceed to realize what you can get out of the security by selling it. For instance, suppose that on January 2, 1904, a man mortgages his house, the mortgage loan to be paid one year from date. If he dies in July, 1904, the mortgagee may start suit to sell the property covered by the mortgage after the loan falls due in the beginning of the year 1905. The ordinary unsecured creditor, on the contrary, cannot enforce payment of his claims, even if the estate is solvent, until one year has elapsed from the granting of letters. Interest runs on each claim from maturity, for it would be unjust to make a creditor lose a year's interest merely through the debtor's death.

This matter of *interest* reveals another distinction between the rights of creditors of the estate and the rights of beneficiaries. If a friend of the decedent has been left a legacy of \$1,000, the legacy will not carry interest from the date of the decedent's death, but only from one year after the death. In a few cases, where the particular beneficiary has stood in the position of a child by birth or adoption towards the testator, the courts have construed provisions of various wills to mean that the testators intended to look after the present

maintenance of the beneficiaries, and have allowed interest to begin immediately from the death of the decedent. The entire subject of interest to be paid by decedents' estates is one over which the Orphans' Court exercises a greater or less degree of supervision. Questions of interest are often decided in the light of particular circumstances. For instance, the Orphans' Court has a wide discretion in the matter of surcharging an executor with interest. Sometimes a delinquent executor will be ordered to pay interest on funds which have lain idle in his hands long after they should have been distributed, but a long delay in making distribution is frequently excused for any good reason.

If there is any doubt as to the validity of a claim, the executor should not pay it, but should insist upon the claimant's proving it before the Orphans' Court, or before the auditor who is specially appointed in the counties where there are no separate Orphans' Court judges. The alleged creditor is entitled to the benefit of a jury trial, and may commence an action at law in the Court of Common Pleas against the executors. Comparatively few creditors resort to a jury trial, however, because the Orphans' Court will pass upon the merits of the claim, and settle the matter quite as justly and more speedily than if it goes on the trial list in the Court of Common Pleas. The Orphans' Court auditing judge decides issues of fact and of law and is guided by the same rules of evidence as govern in the Courts of Common Pleas. Where the alleged contract is verbal, the death of the decedent renders the surviving party incompetent as a witness. It will be necessary, therefore, for the claimant upon a verbal contract to depend upon others to substantiate his claim, although the objection as to the incompetency of the claimant himself may be waived, if the representative of the estate so desires, and the court approves. If, however, those interested in the estate insist upon strict compliance with the rules of evidence, the claimant cannot offer verbal evidence at all. It is far better to have a written contract, because so many attempts are made to loot the estates of the dead that the Orphans' Court is on its guard against

trumped up claims, and always views with especial suspicion the presentation of a claim after a man has died which has not been presented in his lifetime, in case the claimant had a good chance to present it during the life of the decedent himself.

(C) Payment of collateral inheritance and other taxes.

An executor should pay all taxes for which the decedent was personally liable at the time of his death. Such taxes may be considered as debts due by the decedent. The matter of taxation which mainly concerns most executors and administrators is the tax on collateral inheritance. This deserves separate treatment, because the tax is really payable, not by the estate, but by certain beneficiaries who get a share out of it. The executor or administrator, however, is bound to attend to the payment of this tax. If he were permitted to make distribution to the beneficiaries without deducting the tax, many of them would neglect to pay it, and the state would, perhaps, find it difficult or impossible to force them to do so.

The act of May 6, 1887, provides that all estates, real and personal, situated within this commonwealth, whether the purchaser dying possessed thereof had his home here or not, shall be subject to a tax of 5 per cent on all the property which passes to any persons or corporations, except the father, mother, husband, wife, children, grandchildren, great-grandchildren, and other lineal descendants born in lawful wedlock, or the daughter-in-law of the decedent. This is called a collateral inheritance tax, because it affects only those who take as collaterals, and not those who take as direct descendants of the decedent. Not only the direct descendants, but also the parents and the husband or wife, and the daughter-in-law of the decedent are spared. The daughter-in-law is exempted, whether or not the decedent's son is still alive. The amendment of April 22, 1905, exempts children of a former husband or wife of the decedent. The act of 1887 attempts to extend the tax to all property of Pennsylvanians which is located outside the state. This attempt is

unsuccessful, except in certain peculiar cases, for foreign real estate is not taxable here. *Bittinger's Estate* (1889), 129 Pa. 338. See, however, *Miller v. Commonwealth* (1886), 111 Pa. 321, and *Coleman's Estate* (1893), 159 Pa. 231.

The entire estate coming into the executor's hands is not subject to this tax, even though there are no near relatives. Suppose a man dies, leaving \$100,000, but with \$50,000 of debts. Suppose all his property is to go to a cousin. The 5 per cent would be calculated upon the net amount which would actually be received by the cousin, after deducting the cost of administering the estate and the \$50,000 indebtedness, so that the amount of collateral inheritance tax would be a little less than \$2,500.

If the collateral inheritance tax is paid within three months after the decedent's death, a deduction of one-twentieth part of the tax is allowed. If the tax is not paid at the end of one year from the death of the decedent, interest is charged at the rate of 12 per cent per annum. Where, however, by reason of claims made upon the estate, litigation, or other unavoidable cause of delay, the estate cannot be settled at the end of the year, only 6 per cent is charged from the end of the year until the cause for delay is removed. As soon as the cause for delay is removed the tax must be paid or the rate will then be 12 per cent. If property is tied up by litigation, and does not produce 6 per cent of its real value, the interest on the tax is to be reduced accordingly.

When the executor or administrator qualifies, he takes an oath that he will comply with the collateral inheritance tax. If he delays paying it for over a year, and through his negligence the estate is obliged to pay interest to the commonwealth, he may be surcharged with this interest. He should pay the tax on all the net assets, which will go to the non-exempt beneficiaries under the will, or to the collateral relatives under the intestate laws if there is no will. Suppose ten shares of stock, appraised for taxation at \$60 each, are left to a cousin. The executor should pay \$30 to the state as the tax on this bequest, and collect it from

the cousin when he turns over the certificate for the ten shares. Let us imagine another case. Suppose \$1,000 are left to each of the five nephews of the decedent. After paying all debts, the executor finds that the nephews get only \$500 apiece, on account of a shrinkage in the value of the estate. Of course, the tax will be calculated upon the net sum passing to each nephew, so that the executor will give each nephew \$475.

The act of 1887 provides that no estate which may be valued at less than \$250 shall be subject to the tax. The decisions on this matter are somewhat in conflict. The idea of the courts seems to be that if the entire amount passing to collaterals is less than \$250, then the estate is not subject to a tax, even though the children of the decedent may have received thousands of dollars and the creditors of the decedent may have received thousands of dollars also. Suppose the only provision for collaterals made in a man's will is that \$200 shall be given to each of his two domestic servants. The sum of \$400 would be subject to the tax, and the executor would have to pay \$20 to the state. If one of the two servants had died before the decedent, only \$200 would pass to collaterals, so that the state would get nothing at all, although the property coming into the executor's hands might be worth millions.

It is frequently annoying to have a number of legacies pared down by the deduction of this 5 per cent tax. It disappoints the legatees, and makes a lot of additional figuring and odd numbers. To avoid all this, some testators, when making a number of charitable bequests and gifts to friends and distant relatives, provide that the estate shall pay the collateral inheritance tax, and that the legacies shall be paid in full and free of the said tax.

The tax is paid to the Register of Wills of the county where the estate is settled, who forwards the money to the State Treasurer. The executor should be very careful to preserve the receipts for these taxes, because the judge or auditor who examines his account may insist upon the production of the original collateral inheritance tax voucher.

The payment of this tax often involves some fine calculations in determining the value of life interests which are subject to taxation. Suppose property is left in trust for one person during his life, and upon his death the property is to go to the children of another person. The value of the life interest which is subject to the 5 per cent tax requires careful computation, and resort is frequently had to actuaries' insurance tables.

If the estate is settled in Pennsylvania, the executor must pay the tax on all the personal property which comes into his hands, even though some of it may come from a distant state. Where a foreign executor transfers in Pennsylvania any stocks or bonds standing in the decedent's name, which are liable to the tax, a statute requires the tax to be paid to the Register of Wills of the county where the transfer is made at the time of the transfer, otherwise the corporation permitting the transfer becomes liable to pay the tax. This statute is seldom attempted to be enforced.

The Register appoints appraisers to value the property subject to the state collateral inheritance tax, and usually there is no trouble about getting a fair appraisal. If any person affected by the appraisal is dissatisfied with it, he has the right to appeal to the Orphans' Court within thirty days after it is made.

(D) Advancements.

Sometimes it appears that the decedent has set up one of his sons in business, or given him a large sum of money with the intention of letting him reap the immediate benefit of it rather than to postpone all division of his estate until after his death. The act of 1832 directs as follows: If any child of an intestate shall have any property settled on him by the intestate, or *advanced* to him by the intestate during the latter's life, and the property is equal in amount or value to the share which shall be allotted to each of the other children of the intestate, such child shall take no share in the estate. If the amount of the settlement or advancement is less than the share to which the child would otherwise be entitled, then

the amount of such settlement or advancement shall be deducted from the share of the estate going to such child, so as to make all the children equal sharers in the estate. This act makes the question of advancement largely a question of intention, which may be shown by the character of the transaction and the surrounding circumstances. Usually advancements are made by parents, but a grandparent may stand in the relation of a parent, in such a way as to make his gift to one of his grandsons count under certain circumstances as an advancement, with the result that the particular grandson's distributive share of the estate will be afterwards reduced by the amount of the advancement. For instance, in one case a grandfather gave his grandson a very large sum of money to enable the latter to engage in a permanent business. The amount thus given was equal to two-thirds of the grandson's share in his grandfather's estate. Nothing was said or done when the money was transferred or afterwards to indicate clearly what was the grandfather's intention. The Supreme Court decided that the large amount of money involved and the purpose to which it was to be devoted proved that the grandfather must have intended it as an advancement on account of the grandson's share in the donor's estate when the grandfather should die.

Money furnished by the parent for the child's education will not be presumed to be an advancement without clear proof that such was the parent's intention, because it is a parent's duty to educate his children. Expenditure of money for the maintenance and education of the child is considered to be in the nature of a gift from the parent to the child. An advancement is also a gift in the sense that it creates no obligation upon the child to repay it. It only subjects the child to the necessity of deducting from his distributive share as a beneficiary of his parent's estate the amount of any such payments made to him in the parent's lifetime. The valuation of the property advanced to the child is to be calculated in accordance with the value at the time the advancement was made, and not at the time the parent dies. Interest is not chargeable on advancements

from the date when originally made, but is sometimes charged from the expiration of one year after the death of the parent, because that is the time when the estate should be settled.

(E) Widow's and children's exemption.

The act of April 14, 1851, provides that the widow or the children of a decedent dying testate or intestate may retain either real or personal property belonging to the estate to the value of \$300, even though the estate is insolvent. If the wife has deserted her husband, or if they have lived apart a long time before the husband's death, the woman is not within the spirit of the act of 1851. If the widow dies or remarries before her claim is first presented it is too late to make it afterwards. The widow is ordinarily entitled to the exemption even though she has ample means of her own. Her claim will be preferred over claims for the funeral expenses of the decedent or for medical attendance.

Where there is a widow the children cannot claim the exemption. It is intended to relieve the immediate wants of the family, but the money is paid to the widow, and it is presumed that she will use it properly. She is responsible to no court, except the court of conscience, if she fails to use it properly. Where there is no widow, children who constituted the decedent's family at the time of his death are entitled to the exemption. In some recent cases the exemption has been granted to full grown children, even though they were not dependent for support upon their father, provided they were members of his household. The claim for exemption may be made to cover articles of personal property or real estate, and sometimes certain items of personal property will be claimed, and the rest of the \$300 will be claimed out of real estate. No time is absolutely fixed by law within which the claim must be made. It should be made within a reasonable time, and this varies with the circumstances of each particular case. If a long delay has wrought such changes in the estate that expense and embarrassment would result from allowing the claim,

it would be unfair to allow it. Where, however, a delay of over a year was found not to have prejudiced the interests of any parties, the lapse of that length of time was held not to bar the widow. Where the estate is solvent a longer time will be allowed than where it is insolvent. Again, if the widow is feeble and illiterate, she will be given a longer time than if she is capable and well informed.

She should make a formal demand upon the executor or administrator, and present a petition to the Orphans' Court, asking the court to award the articles claimed by her for her own use and benefit. With this petition should come an inventory and appraisal of the goods claimed by her, which should be made under oath by the same appraisers as have appraised the decedent's personal estate. If she is to get her exemption in cash, no appraisal is necessary. If she claims her exemption out of real estate, a difficulty may arise in case the real estate is worth more than the sum of \$300. If the real estate is worth more than \$300, but less than \$600, and it appears that it is impossible to divide the real estate without spoiling it, the Orphans' Court may award the entire real estate to the widow, upon condition that she pay the amount of the appraisal in excess of the \$300 exemption within one year. If she refuses to do this, the real estate may be sold.

CHAPTER LVIII.

THE ACCOUNTS OF EXECUTORS AND ADMINISTRATORS AND THE FINAL STEPS IN CLOSING AN ESTATE.

Under ordinary circumstances an administrator or executor should make up and file his account upon the expiration of twelve months after he has received letters. If he files his account prematurely, that is to say, at some time within a year after letters were granted, the court usually refuses to order distribution until twelve full months have elapsed, because creditors are supposed to have that length

of time in which to present their claims. If the executor delays more than twelve months in filing his account he is likely to be besieged by those interested in the estate who will clamor for their money, and blame him for the delay.

Suppose the executor has failed to file his account after the lapse of a year from the time he qualified. As a rule a good-sized period of grace is allowed, and the parties who want the account to be filed usually content themselves for several months with requesting the executor to make haste. Sometimes they let years go by without taking any action. They have a right, however, after the expiration of a year, to petition the Orphans' Court for a rule upon the executor, requiring him to show why he should not file an account. The Orphans' Court will grant this petition, and a copy of it must be served on the executor. If the executor does not give any reasonable excuse for further delay, the court will order him to file an account usually within ten days after notice of the order is served upon him. If the executor replies under oath that he has not received any assets, he will not be obliged to file an account, unless the other side can prove that he has received assets. Suppose that the executor has not made any excuse at all, or has urged some insufficient excuse for his failure to file an account, and the court has ordered him to file one. If he does not do so within the time allowed he is in contempt of court. If the court wishes, he may be committed to jail in order to enforce obedience. The Orphans' Court, however, is averse to this drastic procedure, and prefers to have an auditor appointed to state an account on behalf of the delinquent executor.

This auditor hears testimony about the assets which have come into the executor's hands, and states an account, charging the executor with such assets, and crediting him with all proper payments that he proves to have been made. The costs of the audit are usually charged to the executor himself, since it has been through his fault that they were necessitated. The report of the auditor is finally completed, and he notifies the executor and others to inspect it at his office. All parties have a right to examine it at the auditor's

office, and to notify him of mistakes in it. If one of the parties takes an exception to anything in the account, and the auditor thinks that the exception is based on good grounds, he amends his account accordingly. If he thinks that there is no ground for the exception, he sends the account at the end of ten days, together with the exception, to the Orphans' Court. If no exceptions are made within ten days, it is usually too late to make them afterwards. After the auditor has filed an account in the Orphans' Court, supposing that no exceptions have been taken, it is confirmed absolutely after about three weeks, and is just as valid in all respects as if the executor himself had filed it, and the Orphans' Court had passed upon it.

(A) Auditing the account.

It is the practice in some counties of Pennsylvania, where there are no special Orphans' Court judges, to send most accounts which have been filed by executors to lawyers, who are appointed auditors by the courts. The proceedings before an auditor under these circumstances are very much like those described in the preceding paragraph, except that the auditor is appointed to examine the executor's account, rather than to state one for him. Let us follow the course of an account which has been prepared by the executor or administrator in a county where there are separate Orphans' Court judges. In the first place it is filed with the Register of Wills. At the time the account is filed certain fees are paid to the Register of Wills, varying in amount with the size of the estate, as shown by the account itself. The account is recorded in the account books kept by the Register, and is advertised once a week for four successive weeks in at least two daily papers. The rules of some courts require certain additional advertising. Then it is sent to the Orphans' Court, along with all the other accounts that are fully advertised and in readiness for auditing. The audits are advertised twice in three or more daily papers, and in such other publications as the rules of court may prescribe.

When an account is called for audit, the first question that is of much prominence is whether or not there is any contest. If there is a contest, the matter is sometimes put off until another day, when there will be plenty of time to hear it at length. In most cases there is no contest, and the proceedings are very brief. The attorney for the estate in some counties hands to the auditing judge a statement under oath setting forth the date of the decedent's death, the names and relationship of the persons who claim a share in the distribution, and the names of their guardians, if any of them are minors. Certain other facts appear in this statement, which is to enable the judge to make his adjudication properly. It is best to have all the accountant's vouchers ready, although in many cases the court does not look at them. Where the accountants charge themselves with the amount of the inventory and appraisement, a copy thereof should be submitted to the auditing judge. Sometimes judges find it necessary to conduct audits upon the presumption that if there is anything wrong with the account, those interested will probably expose it. The immense amount of business transacted in many Orphans' Courts precludes the judges from going personally into each question. They must depend in many matters upon the vigilance of those who are interested in the estate for the discovery of anything wrong. Often, however, some glaring blunder or flagrant wrongdoing will be revealed by a casual inspection to the trained eye of an Orphans' Court judge. It is far better, however, for those who are going to get anything out of the estate to learn when the account is first filed and to go over it carefully in order to prepare themselves long beforehand for asserting their rights at the audit and exposing the executor, if he has been guilty of anything crooked. In comparatively few cases, however, is there any question of positive fraud, but there are many cases where mistakes have been committed. The executor's attention should be called to these mistakes, and he will probably agree to rectify them without a contest.

The executor should be prepared at the audit to substantiate all payments for which he claims credit with proper vouchers. He should also be able to prove that the debts and claims which he has paid were legally enforceable against the estate. He should beware of paying anyone whose claim is not strictly legal merely because he sympathizes with the claimant. In *Barhite's Appeal* (1889), 126 Pa. 404, an executor, Alexander Barhite, was surcharged with a large sum which he had improperly paid out of the estate of his father, John Barhite. The latter left an estate worth almost \$100,000. Alexander Barhite's daughter had kept house for her grandfather, performing all the ordinary household duties, and occasionally assisting him in the outside work on his large farm. He furnished her with clothing, but she never demanded or received any money from him. He was unable to read or write, and she rendered him very valuable aid in the transaction of his business, computing interest for him and keeping his affairs in shape. While there was no evidence of an express contract of payment, it was testified that when John Barhite sent the request for his granddaughter to come and live with him, it was accompanied by a statement that he would pay her. There was also testimony that in speaking of her services in his financial affairs he had frequently said that he did not know how he could get along without her, and that he intended to pay her well.

Referring to these statements, the Supreme Court said that they were only loose declarations which can almost always be proved in such cases, and which refer to future intentions. They do not indicate a binding contract, but are vague expressions which may mean a provision by will to remunerate the services, or some other benefit to be conferred in any one of various ways. The lapse of nine years during which the claimant had lived with her grandfather without any demand for or receipt of a single dollar strongly told against the possibility of a contract. The Supreme Court said that the sum claimed, \$3,675, was quite excessive, and that they were disposed to discourage such claims

against decedents' estates. The executor was, therefore, surcharged with the amount paid to his daughter.

Alexander Barhite debited himself in his account with the sum of \$4,000 which he had owed to his father at the time of the latter's death. He claimed the same commissions on this sum as on the rest of the estate which he had collected from others. Commissions were disallowed on the amount of his own debt to the estate. He did not collect this, for he already had it in his possession as debtor. Where an executor owes money to the estate, he should promptly deposit the amount due by him to the credit of the estate with the other funds which he holds as executor. If he fails to pay his own debt until the time when he files his account, he may be charged with interest.

Let us look at some of the expenses of administration which may become the subject of a contest. First, let us see about charges for the services of an accountant. Usually an executor draws up his account himself or gets his attorney to do it for him, but suppose he retains a *certified public accountant* to prepare his account for audit. May he charge for the services of this accountant? He may not do so in the case of the ordinary estate which does not involve difficult accounting. If the estate is very large, and there are a number of complicated items, the rule is different. The practice of employing accountants in such matters is growing, and in this, as in all other matters, the courts adapt themselves to custom. The charge for an accountant's services may, therefore, be made where it seems reasonably necessary to employ assistance in preparing an account. The charge for services of other agents stands on the same basis, but the court is not disposed to let an executor put all the work on employees, and then recover his own commissions as well as the outlay for the services of these employees. Where the employment is reasonably necessary, however, the outlay may usually be charged to the estate.

The services of an *attorney at law* are considered proper in the settlement of every estate. The charge for these services will vary widely in accordance with the amount of

work and the size of the estate. If there has been litigation, the expenses of such litigation are chargeable against the estate, unless the executor has acted imprudently in undertaking the litigation. The mere fact that a lawsuit brought by the executor has not been successful and that the beneficiaries expressed their disapproval of it from the beginning does not deprive the executor of his allowance for counsel fees and costs in the matter. The executor is bound to look after the interests of the estate, and if he does so faithfully and carefully he will not be punished merely because things do not turn out successfully. In one case a will provided that its terms should be carried out under the direction of a certain named attorney, but all the executors were legatees, and a serious conflict arose among them. Their individual interests were opposed to those of the estate in certain matters, and it seemed proper for them to employ separate counsel. Under the circumstances an allowance for all of the counsel was made from the estate because all had been retained for the benefit of the estate. Where there are several executors, they cannot ordinarily by employing different attorneys make the estate liable for a larger aggregate sum than if they had united in employing one attorney. No set rule regulates the amount to be charged by an attorney for the estate of a decedent. The matter depends entirely on the value of the services, taking into consideration the size of the estate, and to some extent the success or failure of the efforts which the attorneys put forth on behalf of the estate.

Coming now to the question of the *compensation* of the executor or administrator, it may be stated that he is not supposed to make a great profit out of the estate. The word "compensation" indicates that he is to get what may be fairly calculated as the value of his services to the estate in question. The amount is usually regulated according to the receipts. The debit side of his account will, therefore, determine the sum to be charged as commissions. In the case of an estate where the accountant debits himself with, say, \$10,000 or \$20,000, 5 per cent commissions are usually

allowed. If there are two executors, the estate does not have to pay anything more, but each executor gets one-half the regular commissions. Where the estate is very small, a fixed sum may be awarded to the executor instead of commissions. Suppose the estate is only \$300, the sum of \$15 would not be fair compensation to the executor, and he would probably be allowed \$30 or \$40, and perhaps more if his services were extraordinary. If, on the other hand, the estate amounts to say, \$30,000, and the executor's labor has been unusually slight, he may be allowed less than the ordinary rate of compensation, and commissions in such cases are often reduced to 3 per cent. If the estate is very large, the percentage is reduced, but the heavy responsibility incurred by the executor, the nature of the services rendered and other circumstances are considered in awarding commissions. On an estate of about \$100,000 3 per cent is allowed in the ordinary case. If it runs up to \$500,000, no more than 2 per cent would usually be allowed. If the executor has been slightly neglectful, but not grossly so, he is entitled to receive some commissions, but less than he would get under ordinary circumstances. On the other hand, if he has shown extraordinary sagacity in handling the estate, and has by his personal endeavors notably enhanced its value, he will get additional compensation. Where there is no necessity of converting the property into cash, the courts sometimes cut down the usual 5 per cent commissions to 3 per cent. Suppose that a decedent has sold all his property before his death, and the administrator has nothing to do but to distribute among a few persons a fund which he finds in bank. No set rule governs the court under such circumstances, but they may decide to reduce the commissions.

The foregoing statements apply to the personal estate which comes into the hands of an executor, and also to the income from the personalty. The executor should credit himself in the principal account with the commissions calculated on the principal which has come into his hands. In the income account, he should credit himself with commissions on income. A different rate of compensation prevails,

where the executor accounts for the proceeds of real estate. If he has not sold real estate, but has taken charge of it and rendered special services with regard to it, he will not be allowed the same commissions as if he had sold it, but only a lump sum in accordance with the nature of his services. If he has sold it, he will be allowed $2\frac{1}{2}$ per cent commissions in ordinary cases. This may be increased to 3 per cent if the special conditions of the case warrant the increase. If the real estate sells for \$100,000 or \$200,000, a smaller rate of commissions will usually be allowed. Coming to the question of the income from the real estate, the general rule is that 5 per cent is the proper rate of commissions, subject to increase or decrease under special circumstances. Where there are very many houses from which rent is to be collected, or for other reasons it would not be right to expect the executor to collect the rents himself, he may employ an agent. In one case such an agent was paid 5 per cent by an executor, and as it was considered proper in that case to employ an agent and to pay him the rate named, the executor was allowed 3 per cent for his own responsibility and supervision.

Commissions may be allowed an executor at a partial accounting on so much of the assets of the estate as have then passed through his hands. They are due when the services are performed, and if it would inconvenience the estate for the executor to take the commissions at the time, he may claim interest on them when he files his account, dating the beginning of interest from the time when the services were rendered. As a rule, however, interest should not be claimed by an executor, for the Orphans' Court is disposed to regard his commissions as sufficient compensation. If the commissions claimed by an executor when he settles his first account are not contested, he cannot be surcharged when he files his second account on the ground that the commissions which he took before were excessive. Where the same person is both executor and trustee under a will, he can receive only one commission on the principal of the estate, for it is but one fund that he is handling, first in the capacity

of executor, and then as trustee. As trustee, however, he may claim a reasonable compensation out of the income of the estate which he has paid to the beneficiaries of the trust.

Sometimes an executor will make a special agreement to settle an estate for less than the customary compensation, and this will bind him. If he has been grossly negligent or committed any actual fraud he forfeits his commissions. Ignorance or inexperience, even though it causes some loss to the estate, will not deprive an executor of all claim to commissions. It will, however, make him liable to pay to the estate whatever loss he has caused, if an ordinarily prudent man would have avoided such loss. In one case it was attempted to surcharge an executor because his accounts showed a glaring disregard of the first principles of bookkeeping. He had not acted dishonestly, and his unscientific bookkeeping had not caused loss to the estate, so his commissions were not reduced. If an executor uses the funds of an estate in speculation, and causes loss to the estate, he is not entitled to commissions, even though he has rendered faithful service for many years. The Orphans' Court uses its good judgment on this matter of commissions, and decides each case according to its peculiar circumstances, but upon the basis of the general principles just given. The most important rule for the executor to follow is that he must not use the estate for his own selfish advancement, or make any secret profits out of it. If he puts himself in a hostile position towards the estate, and unsuccessfully presents a claim of his own against it, which is defeated after litigation, this may be a reason for depriving him of compensation, or greatly reducing his commissions.

(B) Form of executor's and administrator's account.

The following is a simple account filed by an administrator *c. t. a.* Most accounts in the Orphans' Court are similar in make-up to the one given below, whether filed by executors or administrators.

IN THE ORPHANS' COURT FOR THE CITY AND COUNTY OF PHILADELPHIA.
ESTATE OF MARGARET JONES, DECEASED.

April Term, 1906.

No. 483.

First and Final Account of William P. Henry, Administrator Cum Testamento Annexo.

DR.

The Accountant charges himself with principal received as follows:

1905.		
June 4.	To amount of inventory and appraisalment.....	\$19,246.19
July 2.	“ gain on sale of 500 shares Philadelphia Electric Co. stock	400.00
	Total	\$19,646.19

CR.

The Accountant claims credit as follows:

1905.		
June 1.	By cash paid Register of Wills for letters of adminis- tration c. t. a.	\$23.50
“ “	By cash paid Register of Wills for two short certifi- cates	1.00
“ 9.	By cash paid Title Guaranty Trust Co., surety on administration bond	45.00
“ “	By cash paid <i>Press</i> Co., advertising letters of admin- istration	6.00
“ 12.	By cash paid Charles Wagner, funeral expenses of decedent	220.00
“ 14.	By cash paid <i>Legal Intelligencer</i> , advertising letters of administration	3.50
“ 15.	By cash paid <i>Philadelphia Item</i> , advertising letters of administration	3.00
“ 19.	By cash paid U. G. I., gas bill due by decedent.....	2.60
July 18.	By cash paid <i>Philadelphia Demokrat</i> Publishing Co., advertising letters of administration	3.00
“ 31.	By cash paid Henry Leamon, M.D., for professional services to decedent	10.00
Dec. 30.	By cash paid John Dunbar, Esq., for professional services	250.00
	Amount carried forward.....	\$567.60

Amount brought forward	\$567.60
By cash paid notary, affidavit to this account and to schedule of distribution	1.00
By cash paid Register of Wills for filing, advertising and recording this account	23.50
By commissions of accountant	982.30
By balance	18,071.79
Total	<u>\$19,646.19</u>

To balance as above, composed as follows:

\$4,000 Electric and People's 4 per cent trust cer- tificates	\$4,000.00
Cash	14,071.79
Total	<u>\$18,071.79</u>

The accountant claims credit in distribution as follows:

1906.

Feb. 2.	Household furniture delivered to William Jones, under provisions of will, as per inventory.....	\$500.00
" 12.	Horse and carriage delivered to Ellen Morely, legatee: inventory value \$500, less \$25 inheritance tax.....	475.00
" "	Legacy to Henry Williams: \$500, less \$25 collateral inheritance tax	475.00
" "	Collateral inheritance tax on the two foregoing items..	50.00
	Balance for distribution	16,571.79
		<u>\$18,071.79</u>

Dr.

The accountant charges himself with income received as follows:

1905.

Oct. 3.	To six months' interest on \$4,000 Electric & People's 4 per cent certificates	\$80.00
1906.		
April 3.	To six months' interest on \$4,000 Electric & People's 4 per cent certificates	80.00
	To interest on deposits	109.74
	Total	<u>\$269.74</u>

Cr.

The accountant claims credit as follows:

Commissions of accountant	\$13.48
By balance	256.26
Total	<u>\$269.74</u>

RECAPITULATION.

Balance as per account of principal	\$18,071.79
Balance as per account of income	256.26
	<u>\$18,328.05</u>

[Signed] WILLIAM P. HENRY.

State of Pennsylvania }
City of Philadelphia } ss.

William P. Henry, the accountant, being duly affirmed according to law, doth affirm and say that the foregoing account is just and true both as to items of charge and discharge.

Affirmed and subscribed before me this
second day of June, A. D. 1906.

[Signed] WILLIAM P. HENRY.

[Notary's seal, signature, etc.]

Some of the following rules are exemplified in the foregoing account. The others may be readily grasped. These rules govern the acts of executors and administrators in most of the counties of Pennsylvania. The first rule is that accounts should be stated with debits preceding credits. Reference to the foregoing form will show that this does not permit an executor to confuse debits of a principal account with those of an income account. The debits of principal should precede principal credits. Then, in the income account, debits will again precede credits. Likewise, if the executor has sold real estate, his real estate debits will precede real estate credits.

The dates of all receipts and disbursements must be accurately stated. Administration must not be blended with distribution. In other words, the items of account which

tell what the accountant has received and what he has paid out to creditors of the decedent, and to pay the costs of administering the estate, must be kept separate from any items showing what he has distributed to the legatees and any other beneficiaries of the estate. This rule distinguishes between all payments to those who have claims against the estate by reason of judgments or contracts, or by reason of torts committed by the decedent, on the one hand, and, on the other hand, those who get something out of the estate merely because they are relatives of the decedent, or have been left something by him under the terms of his will.

Principal must not be blended with income, but a separate account must be given of each. They are both brought into the same general account, but are kept under distinct heads. Real estate must not be blended with personal estate, and if the executor has sold real estate, he must keep the proceeds of it in a separate part of his account. If the balance of personal property is not sufficient to pay the decedent's debts, the executor (or sometimes under the act of March 29, 1832, any other interested party) may apply within two years of the decedent's death for permission to sell his realty. Suppose that this is done. The real estate is sold, and the proceeds are used to pay debts. When the time comes for accounting, the executor may file one account covering all the matters transacted by him. He should begin by debiting himself with all the items of personal property that have come into his hands, and then credit himself with the expenses of administering the estate and payments made by him to settle the decedent's debts. This would mean that the personal estate account would show a deficit. Then he would debit himself in the real estate account with the proceeds of the sale of real estate, and credit himself with the expenses of the said sale. In the recapitulation the deficit shown in the personalty account would be subtracted from the balance shown in the real estate account, and the net balance for distribution would appear.

Where an executor or administrator is also a trustee, and has to do with the same funds in both capacities, he

should be careful not to mingle his accounts as executor and trustee. This rule is more important than the other rules about the confusion of different accounts. Where an account is brief some executors blend principal and income, and if the result of such blending works harm to no one, the court will usually not object. Ordinarily such a mistake is merely a mistake in the form of the account. It is a more serious blunder for an executor, who is also trustee, to confuse his accounts.⁷ The two matters should be kept for entirely different accounts. In the same way, an executor who is also guardian must not exhibit his accounts as guardian in the same document that contains his accounts as executor. Likewise, the account of an administrator *d. b. n. c. t. a.* must not be exhibited with the account of the first executor, because the accountants are really two separate persons.

The title of the account should state what it contains. If the account gives a full and complete statement of all matters connected with the estate, and there is to be no further account, the practice is to entitle it, say, "The first and final account of William P. Henry, executor." If there are to be other accounts, the title sometimes is about as follows: "The first and partial account of William P. Henry, executor." The account proper follows immediately after this title, and usually contains nothing but dates and debits and credits. An affidavit must be made at the end, in which the executor or administrator swears or affirms that the account is just and true. Nobody should make this affidavit on behalf of the executor, unless it appears that for some good reason, as, for instance, extreme illness, the executor is unable to make it himself.

The accountant will frequently debit himself at the beginning of the account with the amount of the inventory. If he has sold some of the goods listed in the inventory at an advance over the inventory valuation, he should, of course, debit himself with the difference. If he has sold some of the articles scheduled at less than the inventory figures, he should claim credit for the difference. When it is feared that some

of the goods may sell for less than their appraised valuations, the executor should usually dispose of these before filing his account, in order that he may credit himself with the difference between the inventory value and the selling price in the account itself. Of course an executor will not be surcharged with the shrinkage if he postpones the sale of the assets until after filing his account, unless he has been guilty of negligent delay. Nevertheless, it is an awkward position for an executor to find himself in when he must explain to the people who want the estate distributed that the balance found due by his account does not consist of cash but contains some articles which have been appraised too high, and the sale of which will result in the reduction of the amount to be distributed.

At the audit of the account, the attorney for the accountant will sometimes hand to the auditing judge a list of additional debits and credits. Where the account is a first and final account, it would be troublesome to arrange about debits or credits which were omitted by mistake or which arose after the filing of the account, unless it were possible to amend the account at the time of the audit. If the additional debits and credits handed up to the judge at the audit are for very large amounts and suggest to him that perhaps they have been omitted purposely from the account filed, he may refuse to pass on them, and may direct that they be made the subject of a future account. Usually, however, no such objection is made to the allowance of the additional debits and credits. It frequently happens that an executor may feel averse to fixing his own compensation or the compensation of his attorney, and may leave these matters to be settled by the court. When determined, they will figure as additional credits, and reduce the balance accordingly.

(C) The discharge, removal or death of an executor or administrator.

We have now followed the progress of an account down to the point where it has been audited. The Orphans' Court judge or special auditor considers all matters as to which

any question has been raised. Where the account has been referred to an auditor, the proceedings after he files his report are practically the same as where an Orphans' Court judge audits the account. We shall follow the steps taken in a case where the account comes before an Orphans' Court judge. The judge prepares what is called the adjudication. If there is no contest, this preparation is usually a matter of no difficulty. The net balance in the accountant's hands after payment of all debts is awarded to the parties entitled under the will or intestate laws. In case the estate is insolvent, the balance due creditors is distributed among them in accordance with the order of priority mentioned in the last chapter. Sometimes where there are a number of creditors or beneficiaries, the calculation of their respective shares may require complicated figuring. In such cases an Orphans' Court judge may make a general adjudication, determining all disputed matters, and finding a certain net balance. He will not go into the detailed division of this balance, but notes in his adjudication that counsel shall prepare a schedule of distribution. Thereupon the executor's attorney usually calculates the various shares into which the balance will be divided. This schedule of distribution is filed in the Orphans' Court, and attached to the adjudication, of which it becomes part. A limited time is then given for those who may be dissatisfied with the adjudication or the schedule of distribution, to file exceptions. If they fail to file their exceptions on time, the adjudication is confirmed absolutely.

If exceptions are filed, that holds up the distribution of the estate, and the questions raised by the exceptions are argued before the court. The court decides either to dismiss or to sustain the exceptions, and the disappointed party may appeal, to the Superior or the Supreme Court, in accordance with the amount of money at stake. If it is decided that an error has been committed, the adjudication or schedule of distribution will be modified accordingly. It may chance that no fault can be found with the decision of the judge against the validity of some claim, but perhaps the claimant will have discovered further evidence after the adjudication. If he acts

promptly, he may present a petition for a rehearing. Such a petition is seldom granted, for the parties are expected to muster all their evidence at the time of the audit, and the matter ought to be settled then and there. In rare cases, however, the judges will permit a claimant to come into court a second time and introduce new evidence.

An executor should not, of course, make distribution until the adjudication and schedule of distribution have been confirmed absolutely. Frequently beneficiaries clamor for immediate payment, but the executor should require them to wait. He should make all those to whom payment is awarded by the adjudication sign a receipt for his own files, and also a formal "order to satisfy the award" for filing in the Orphans' Court. The following is a form of such an order :

IN THE ORPHANS' COURT OF PHILADELPHIA COUNTY.

April Term, 1906. No. 483.

Estate of MARGARET JONES, Deceased.

Sur Account of WILLIAM P. HENRY, Executor.

To the Clerk of the said Court:

Please satisfy of record the award made to Samuel Jones, by adjudication confirmed absolutely on the 30th day of July, A. D. 1906, namely one thousand dollars, the receipt of which is hereby acknowledged. It is agreed that the said William P. Henry may be discharged.

[Signed] SAMUEL JONES.

August 14, 1906.

After the executor has filed the orders, drawn up in the foregoing form, showing that the awards made by the court have been paid, he should present a petition to be discharged. This petition sets forth that he has paid over the funds of the estate in accordance with the adjudication, and that no other assets have come into his hands. It should appear that all those who are interested in the estate are willing to have the discharge granted. Where the executor or administrator has given a bond, with sureties, for the faithful performance of his duties, it should appear in the petition that his sureties are also willing to have him discharged. If the

petition is in such shape as satisfies the court, it will be granted. A decree will be made showing that the executor has fully completed the performance of his duties.

If B is the executor of C, and B dies himself, someone is usually appointed to manage his own estate. This person will have charge of the estate left by B, but he will not have any right to continue winding up C's estate. C's estate is an entirely separate fund from B's estate. B's executor, however, states an account on behalf of B. This account is only a partial account, if we assume that B has died before winding up C's estate. The partial account covers all matters transacted by B during his lifetime. The balance found due by B must be turned over by B's executor to the administrator *d. b. n. c. t. a.* appointed to complete winding up C's estate.

The continued disregard of his duties by the executor as laid down by statute, or his disobedience to the orders of the Orphans' Court will justify the court in *removing him*. If it appears that the executor has been fraudulently dealing with the estate, that is good ground for removal. Evidence of such fraud may be found in the knowing concealment of assets. If the executor tries to put property of the estate out of reach of creditors, and purposely omits mention of the assets in the inventory or in the account which he files, it is strong evidence of fraud. In an old case it was proved that one of the executors of a certain estate had in his possession various papers, accounts and letters belonging to the estate which he withheld from the examination of his co-executors. The latter applied to the Orphans' Court to compel him to give security, alleging that he was wasting and mismanaging the estate. The court decided that the delinquent executor was not acting properly, and ordered him to enter security, as provided by the act of 1832, so as to save the estate from the danger of his defrauding it. The act in question recognizes that an emergency may present itself after an executor has been appointed which may justify the court in requiring special security, even though the executor at the time of his appointment was not required to give any security at all. In

the case referred to the delinquent executor failed to enter security, and finally his letters were vacated and he was removed. *Chew's Estate* (1845), 2 Parsons 153. .

The Orphans' Court will not readily lend its ear to every slight ground of complaint, and dismiss the executor merely because he has erred in some matter of judgment. For most slight offenses it is sufficient to wait until the executor's account is filed, and to surcharge him if he has made a mistake which justifies a surcharge. Usually the court will not summarily dismiss an executor, unless he has wilfully and fraudulently abused his trust or has persisted in disobeying some order of the court.

The act of May 1, 1861, provides that a petition may be made to the Orphans' Court by any person interested in an estate setting forth that the executor, administrator, guardian, trustee or committee is wasting or mismanaging the property under his charge, or that for any reason the interests of the estate are likely to be jeopardized by his continuance in office, or that he is likely to prove insolvent, or has neglected to exhibit true and perfect inventories or to render full and just accounts of such estates. If the court sees fit, a citation to the delinquent executor or fiduciary may be issued, requiring him to appear on a day fixed and to answer the charge against him. If it appears that the charge is well founded, the court may remove him entirely and order him to deliver over to his successor in the trust all the property belonging to the estate that may be in his hands. The same act of 1861 provides also that if the executor or other fiduciary shall become incompetent to discharge his duties by reason of sickness or other visitation, and if it shall appear to the satisfaction of the court that the incompetence is likely to continue to the harm of the estate, the fiduciary may be dismissed, and a new one appointed in his place.

PART II

THE INTESTATE LAW, WILLS AND TRUST ESTATES

CHAPTER LIX.

THE INTESTATE LAW.

Sometimes a will is called a testament, and the man who makes a will is called a testator. If he leaves no will, he is said to die intestate, and the intestate laws of Pennsylvania govern the distribution of his estate, after payment of creditors. Even where a man makes a will, the intestate laws may govern the disposition of part of his property, if the will does not dispose of it all.

The act of April 8, 1833, as supplemented by later legislation, embodies the intestate law of Pennsylvania. It provides that the real and personal property of a decedent remaining after payment of all just debts, and not disposed of by will or by marriage settlement, shall be divided as follows: First, where the intestate leaves a *widow* and issue, the widow shall get one-third of the personal estate absolutely, and a life interest in one-third of the real estate. Second, where the intestate leaves a widow, but does not leave any issue, the widow gets one-half of the personal property absolutely, and a life interest in one-half of the real estate, including the home and buildings appurtenant thereto. A stable attached to a mansion house would be considered as appurtenant to it. Third, where the intestate is a woman, and leaves a *husband*, he gets a life interest in all her real estate. He gets all her personalty absolutely if there is no issue. If there are any children, he must share the personal property equally with them. For instance, suppose there are five children. The husband has a life interest in all the real estate,

but he gets only a one-sixth part of the personal property. This sixth part, however, he takes absolutely.

Subject to the rights of the widow or widower, the property of the decedent, real and personal, is to be distributed in the following order among his *descendants*. First, if the intestate leaves children, and there is no other descendant of a deceased child, the children share equally in the property, real and personal, and take it absolutely. Second, if the intestate survives his own children and leaves grandchildren, but no great-grandchildren or other descendant representing a deceased grandchild, then all the grandchildren share the estate equally. They are all in the same order of descent, and each one has as great a right to the estate as any other. Third, if the decedent leaves great-grandchildren, but no descendants farther removed than great-grandchildren, and all his children and grandchildren are dead, these great-grandchildren divide the estate among themselves, each great-grandchild getting the same share as any other. These first three rules are quite simple. There can be no great difficulty where all the distributees stand on one even plane, and are in the same rank of relationship. Suppose all the children are dead, and there are only grandchildren, and suppose that the matter is not complicated by the death of one of the grandchildren leaving a number of great-grandchildren: in that simple case all the grandchildren are on the same footing. It may be that there are fifteen grandchildren. Suppose five were children of the intestate's deceased son, and the other ten were children of the intestate's deceased daughter. Both the intestate's children have died. There were fifteen grandchildren, and they are all alive at the time of the death of their grandfather, the intestate. Each grandchild gets one-fifteenth of the fund in the hands of the administrator for distribution.

Now let us suppose that the intestate leaves descendants in different degrees of descent. Suppose he had originally five children, of whom only two survive him. As to the three who are dead suppose the situation is as follows: One of the three died childless. Another died before his father,

but left two children who are still alive. The last of the three died before his father, and he also left two children, but both of these two children also died, one of them, however, leaving eight children. The entire situation confronting us, therefore, is as follows: The intestate leaves two living children. These two may or may not have children of their own, but that question need not concern us at all. In addition to the two living children of the intestate, there are two grandchildren, who represent a deceased child of the intestate. There are also eight great-grandchildren, who are the only living representatives of another deceased child of the intestate. These twelve persons represent the four lines of descent which run down from the intestate. The first two lines of descent stop short at the immediate children of the intestate, for these two children have survived him. The third line of descent runs down to a pair of grandchildren who represent a deceased child of the intestate. The fourth line of descent runs down to a band of eight great-grandchildren who represent another deceased child of the intestate. There is inequality in the degree of relationship to the intestate of these various claimants. The law solves the problem as follows: The fund for distribution is divided into four parts. Each living child of the intestate gets one of these parts, because the two surviving children constitute two lines of descent. The two grandchildren who represent a deceased child of the intestate get another fourth part between them. The octette of great-grandchildren who represent the other deceased child of the intestate must share the remaining fourth part among them, and each of these eight great-grandchildren will, therefore, get only one-thirty-second part of the entire fund. As for the child of the intestate who died childless, before the death of the intestate, he does not figure at all in the distribution.

In the case last mentioned the descendants entitled to participate in the estate did not all belong to the same generation. Accordingly they took "*per stirpes*," that is, each claimant's share was calculated with reference to the various lines of descent running down from the intestate. Suppose that an intestate has had four children, two of whom died

before him, leaving no issue. One of the survivors has children and grandchildren of his own. The other surviving child of the intestate is unmarried. The intestate's two surviving children would take one-half of his estate apiece. They would share "per capita," that is, according to the number of claimants. Where all the claimants entitled to participate are in the same degree of descent from the intestate, they take "per capita," and not "per stirpes."

Subject to the widow's or widower's rights, all the property goes to the direct descendants of the intestate. If there is a single descendant, no other relative, even a sister or parent, gets anything under an intestacy. Imagine now that there are no descendants. Either the intestate was never married, or else he has never had children, or else his descendants have all died before his own death. What becomes of his property in that case? Subject to the rights of the widow or widower, if any, the real estate goes for life to the *parents* of the intestate, if they both survive him, or to the surviving parent if only one parent survives him. In case both parents survive the intestate, they are jointly interested in the real estate, but when one of them afterwards dies the survivor succeeds to the entire interest in the real estate for life. The real estate under these circumstances goes to the parents and to the survivor of them only *for life*. The personal property goes *absolutely* to them. See *Gillan v. Dixon* (1870), 65 Pa. 395.

Subject to the rights of the widow or widower and the rights of the parents, the real estate will go as follows: First, if the intestate leaves *brothers or sisters* of the whole blood, and no nephew, niece, grandnephew or grandniece descended from a deceased brother or sister of the whole blood, the property goes to the said brothers and sisters. Second, if the intestate leaves no brother or sister of the whole blood, and no grandnephew or grandniece representing such a deceased brother or sister, but nephews and nieces who are the children of such deceased brothers or sisters, the property goes to such nephews and nieces. Third, if he leaves no brother, sister, nephew or niece of the whole blood, but grandnephews and grandnieces who are children of such deceased nephews and

nieces, the property goes to such grandnephews and grandnieces. Fourth, if the intestate leaves brothers and sisters of the whole blood and also nephews and nieces or grandnephews and grandnieces who are descended from any such deceased brother or sister, the property descends as follows: Every brother and sister receives a share calculated in accordance with the number of surviving brothers and sisters plus the number of deceased brothers and sisters who have left issue surviving the intestate. The nephews and nieces or grandnephews and grandnieces who represent deceased brothers and sisters take a share by representation. They get exactly the same share as their respective parents or grandparents would get if surviving. Suppose there are two brothers and one sister who survive the intestate, and also three nephews who represent a deceased brother, and two nieces who represent a deceased sister. The estate is divided into five parts. The surviving brothers and sister get one-fifth apiece. The three nephews get one-fifteenth apiece. The two nieces each get one-tenth of the estate. Fifth, if there are no brothers or sisters of the whole blood and no children or grandchildren of any such deceased brother or sister, the real estate vests in any descendants of the brothers and sisters of the whole blood more remote than grandchildren. The personal estate is always divided without reference to whether the claimant is of the whole blood or merely of the half blood, but except for this difference it follows the course outlined in the present paragraph for the descent of realty.

We have seen the difference between distribution "per capita" and distribution "per stirpes." No representation "per stirpes," in accordance with the lines of descent, is allowed amongst collateral relatives after the grandchildren of brothers and sisters or after the children of uncles and aunts, except in certain cases under the act of May 25, 1887, when a grandparent and the descendants of a deceased grandparent are the nearest surviving relatives of an intestate. Let us illustrate this rule which forbids representation among distant relatives. Suppose the nearest relatives of an intestate are his nephews and nieces, of whom six survive him. Suppose one of his nephews died before him, leaving only

grandsons, who are great-grandnephews of the intestate. The property would be divided only among the six surviving nephews and nieces, for the law will not allow the great-grandnephews to take by representation of their deceased grandfather. If he left only great-grandnephews and great-grandnieces, they would take the estate, but since he has left nephews and nieces, the great-grandnephews are not allowed to represent a deceased nephew.

Now let us suppose that there are no descendants either of the intestate himself or of his brothers and sisters of the whole blood, and that all his brothers and sisters of the whole blood died before the intestate. What is to become of the real estate in case the father or mother of the intestate is still alive? In most cases they receive only a life interest in the real estate, but if there are no relatives surviving in the degrees of relationship just mentioned, the interest in the real estate which the surviving parent receives is increased from a mere life estate to absolute ownership. At this point in the course of descent of real estate, the rule that takers must be of the first purchaser's blood begins to operate. This rule is explained later in the present chapter. It applies not only to the intestate's father and mother who claim absolute ownership in his lands, but also to the classes of persons mentioned in the following paragraph. The rule has no application to the descent of personal property.

In default of issue, and also of brothers and sisters of the whole blood and their descendants, and also of father and mother surviving, the real estate descends to brothers and sisters of the half blood of the intestate, and their issue, in the same way as is provided in the case of brothers and sisters of the whole blood and their descendants. In default of all persons hereinbefore mentioned, the personal estate of the intestate is distributed among the *next of kin* generally, and the real estate among the next of kin of the first purchaser's blood.

Where the relatives previously named do not exist, it becomes necessary to look among the next of kin for a person to take the estate, and to calculate the respective rights of distant cousins. The rule which we shall take up now is

one which applies only when it is necessary to search among the distant relatives, and when the descendants before mentioned do not exist, or are not entitled to take under a legal principle of inheritance, hereafter to be mentioned, concerning "the blood of the first purchaser." The rule in question by which to arrive at the nearest relative is to take each claimant and find who was the nearest common ancestor of both the respective claimant and the decedent whose estate is to be distributed. In the case of a second cousin, whose father was the first cousin of the intestate's father, you would have to go back to the great-grandparents of the intestate in order to find one who was an ancestor of both the second cousin and the intestate. Then you would count the number of links in the chain of relationship connecting the intestate and the second cousin. Counting up from the intestate to his great-grandfather, and then down again along the other line until you come to the second cousin, you would have to count six links. If it happened that a son of the intestate's great-grandfather was still surviving, this son, of course, would have a better claim to the estate than the second cousin. Counting the links between the intestate and this son of his great-grandfather, you would have only four links, that is, the first up to the intestate's father, the second up to the intestate's grandfather, the third up to the great-grandfather (who is the common ancestor), and the fourth stretching down to the son of the great-grandfather.

Amongst the next of kin the grandfather or grandmother has the best claim, for they are only two degrees removed from the intestate. In case one or more grandparents of the intestate are living, and also other descendants of any deceased grandparents, the other descendants are entitled to share, *per stirpes*, with the surviving grandparents. The precise method of calculating the respective shares of the parties in various contingencies is set forth by the terms of the act of May 25, 1887.

In default of all of the classes above mentioned, the real estate of the intestate vests absolutely in the widow or widower. At the very beginning of the list of distributees the widow and

widower figure, but the widow usually gets merely a life interest in only a part of the real estate, and the widower merely a life interest in the whole real estate. The widow usually gets only a portion of the personal property, but, in default of all the classes above mentioned, she takes the entire personal estate. Very distant relatives may fall heir to an intestate's real estate before the absolute right of the widow or the widower to become the complete owner of it accrues. It is important, therefore, for a man who has no descendants to make a will giving his real estate absolutely to his wife, unless he wishes it to go in the manner outlined above. The same thing applies to a woman who has a husband but no children or other direct descendants, for if she dies intestate her husband will have only a life interest in the real estate, and perhaps some remote relatives, whom she may care nothing about, may take it after her husband's death. Her husband will not have the right to sell it, and so enjoy the full value of it.

Supposing that there are no next of kin of the first purchaser's blood, and the surviving wife or husband wants to make sure of the absolute ownership of the intestate's realty, what is to be done? An application may be made to the Orphans' Court setting forth the facts. The Orphans' Court, after requiring that public advertisements shall be made, may, in case no relative of the decedent turns up, make a decree setting forth the facts, and this will help to establish a clear title to the realty in the surviving widow or widower. In default of all the classes above mentioned the next of kin who are not of the first purchaser's blood may take the real estate. This class inherits only when there are no other relatives in the prior classes and no surviving widow or widower.

The rule which gives a preference to the relatives who are of the blood of the ancestor from whom the intestate derived the realty is rooted in the old English custom of transmitting real estate in the same family for generations. Upon the failure of direct heirs, the collaterals who take the inheritance are those of the line from which it originally sprang. For instance, suppose an intestate's nearest relatives are two first cousins. One is related to him through his paternal grandparents, and

the other is related to him through his maternal grandparents. If the intestate has received a large tract of land which has come down through his father's family for generations, it is only fair to give the first cousin, who is related through the intestate's father, the full benefit of this inheritance. The other cousin would get nothing, so far as this particular real estate is concerned. Even if the nearest relative on the father's side were a second cousin, he would take the real estate (but not the personalty) left by the decedent, in preference to the first cousin on the mother's side. The only chance for the first cousin on the mother's side to inherit that land would lie in the entire extinction of the father's line. In such a case there is nothing to do but to give the real estate to those who are not of the father's blood. If the intestate has bought the land himself, this distinction between relatives on the side of the ancestor from whom the property was derived and other relatives has no place at all.

In case there is no surviving widow or widower, and no kindred of any description, the *State of Pennsylvania* takes the property. This is called *escheat*. There are some who make it a regular business to watch for the death of wealthy persons, dying intestate, in order to see if it may not happen that there are no relatives. In such a case the person who first informs the Auditor General in writing that the escheat has occurred, and who procures evidence to substantiate the fact, and prosecutes the matter, is entitled to one-third of the net proceeds of the escheated estate. He should sign the letter of information, and have it witnessed by two credible persons. If, however, the escheat proceedings are not started within twenty-one years after the intestate's death, it is too late to institute them subsequently, if the property was in the decedent's possession at the time of his death.

The following is a summary of the order of inheritance of real and personal estate in case of intestacy: (1) *Widow*, if issue, one-third of real estate for life and one-third of personalty absolutely; if no issue, one-half of real estate for life and one-half of personalty absolutely. Or, *widower*, all real estate for life and an equal share with issue in personalty abso-

lutely, (all the personalty absolutely, if no issue). (2) *Issue* to remotest generation; representation. (3) *Father* and *mother*, life estate in realty; personalty absolutely. (4) *Brothers* and *sisters*; representation among their children and grandchildren [as to realty, brothers and sisters of the half blood fall into class (7)]. (5) *Descendants of brothers and sisters* more remote than grandchildren, without representation.

Then (subject to the provision as to real estate that the takers must be of the first purchaser's blood): (6) *Father* and *mother*, real estate absolutely. [As to personalty, see (3)]. (7) *Brothers* and *sisters* of the *half blood*, real estate as in (4) and (5). [As to personalty, brothers and sisters of the half blood share with those of the full blood, as in (4) and (5)]. (8) *Next of kin*; representation to remotest generation among descendants of grandparents, if any grandparent survives; otherwise, representation only among children of uncles and aunts. [See (10) for those not of first purchaser's blood.]

Finally, without qualification as to blood of first purchaser: (9) *Widow* or *widower*, everything absolutely [see (1)]. (10) (As to real estate) *next of kin*, as in (8). [As to personalty, see (8).] (11) Escheat to the Commonwealth.

If a New Yorker dies intestate leaving real estate situated in Pennsylvania, the devolution of that real estate follows the Pennsylvania law, and not the New York law. In the case of personal property, that may ultimately go to New York, and be distributed in accordance with the New York intestate law. Again, suppose the New York testator leaves a will, but does not completely dispose of all his property in it. He is intestate as to what his will does not dispose of. If he leaves Pennsylvania real estate undisposed of, the realty will descend in accordance with Pennsylvania law. Where, however, a man puts a residuary clause in his will, giving all the rest, residue and remainder of his estate to a certain person, that person takes the entire balance of the estate. Suppose the will were made in 1900, and the testator acquired valuable property in 1901, and died in 1902. The will would speak as of the date when he died in 1902, and the man who was left the residuary estate would get the benefit of the

property acquired by the testator in 1901, after the date of the will, unless the testator specifically provided otherwise. Sometimes a man makes certain provisions in his will, and then says that the rest of his property is to be distributed in accordance with the intestate laws. In one case a testator gave his lands to the persons entitled under the law of Würtemberg, Germany, and, of course, the Pennsylvania court ascertained the Würtemberg intestate laws, and distributed the property accordingly.

CHAPTER LX.

WILLS.

(A) General statutory provisions.

There is little or no difficulty about most wills. The courts are not disposed to be very technical in interpreting wills, except in a few peculiar matters, for they understand that these documents are often drawn up by people who are unfamiliar with the rules of law. Some of the wills which are admitted to probate are full of misspelled words and grammatical errors, but the Orphans' Courts do not care about these mistakes, if it is possible to grasp the testator's intention from the terms of the will itself. One point, however, should be known by every person who may want to make a will or who may be called in to witness the making of one. *The testator should sign the will at the end thereof.* The act of 1848 provides that every will should be signed by the testator at the end, or subscribed with his name by his direction and authority, or marked at the end with the testator's mark or cross. This indicates that the will should be in writing. Sometimes wills are typewritten. That method is subject to the disadvantage that a typewritten page may be, perhaps, easily abstracted, and another typewritten page substituted containing different provisions. Where the will is typewritten, it is better to have the testator sign his name along the margin of each page, as well as at the end of the

will. If there are any clauses in the will regarding the disposition of the testator's property which are put after the signature, the will is invalid. The witness clause may follow the signature, and as a matter of fact it usually does come afterwards. Again, if the testator subsequently attaches a codicil which he fails to sign after his signature to the original will, the subsequent codicil cannot be regarded as a part of the will, so far as to invalidate it on the ground that the testator's signature was not put at the end. An unsigned codicil is not itself valid. Not only the will, but also every codicil should be signed at the end. The act of April 8, 1833, provides for the disposition of personal property by a *nuncupative* will, that is a will which is made without writing or signature. This kind of will is good only when made by a testator in the extremity of sickness, and under conditions affording no opportunity of making a written will. The act provides that such a will must be made by the testator in the house of his habitation or dwelling, or where he has resided for the space of ten days or more next before the making of such will except where the testator shall be surprised by sickness when away from his house, and shall die before returning thereto. Where the sum or value bequeathed shall exceed \$100, it must be proved that the testator at the time of making the verbal bequest bade the persons present, or some of them, to bear witness that such was his will, or to that effect; and in all such cases the foregoing requisites shall be proved by two or more witnesses who were present at the making of the nuncupative will. Such a will should be reduced to writing within six days after the testator has verbally made it, in order to prevent the possibility of the witnesses forgetting the exact terms which the testator used. There is an additional reason for requiring a prompt reduction to writing of the nuncupative will, for this requirement eliminates many attempts which might otherwise be made by disappointed persons to trump up nuncupative wills, when in point of fact none were made. *Megary's Estate* (1904), 25 Super. 243.

The act of 1833 provided that any mariner who is actually at sea, or any soldier who is actually in military serv-

ice may dispose of his movables, wages and personal estate without the requirement of writing, and without strict compliance with the requisites of the ordinary nuncupative will. This exception is to meet the case of persons who are away from home, and subject to perils and sudden death, and who may be far away from lawyers, and even without writing materials. *Smith's Will* (1865), 6 Phila. 104.

In Pennsylvania it is not necessary that any witness should see the testator sign his name to a written will, or hear the testator state that he has made it. It is highly desirable, however, to have two or three witnesses put their signatures at the bottom of the will. In some states more formality is required than in others, and it may be that a Pennsylvania testator will when he dies own real estate in some of the states which require that a devise of realty must be very formal. The following specimen of a witnessing clause is one which is suitable for most wills. It is better to have three witnesses sign it, although in this state two are plenty, and none is really necessary. The form referred to is as follows: "Signed, sealed, published and declared as his last will and testament by John Smith, the testator aforesaid, in the presence of us, who, at his request, and in the presence of him and of each other have hereto set our names as witnesses the day and date of the said will." In order that a will may be proved in Pennsylvania it is necessary to have two or more witnesses come to the office of the Register of Wills. If there were no subscribing witnesses, whose signatures appear on the will itself, any witnesses who are familiar with the testator's handwriting will suffice. Sometimes it is impossible to discover any such witnesses, and the alleged will cannot be admitted to probate. If there have been subscribing witnesses, they must appear before the Register of Wills. If they are dead or cannot be found, then, strangely enough, the proof of handwriting concerns not the testator's signature, but the signatures of the subscribing witnesses. Other witnesses must, therefore, be brought forward in order to prove that the signatures of the subscribing wit-

nesses are genuine, and when that is done the will is admitted to probate.

One should be extremely careful in executing *a will which gives property to a religious or charitable corporation*, or in trust for religious or charitable uses. Any provision of this sort in a deed or will is void unless attested by two credible witnesses, who are disinterested at the time the deed or will is executed. The executor is a disinterested witness within the terms of the act making this requirement. Furthermore, the gift to charity or religion must be made at least one calendar month before the death of the testator or settlor of a trust. The residuary legatee or devisee, or the nearest relatives or heirs get the benefit of the void gift, in case the provisions of this act are not strictly complied with. If, however, such disposition of property to charity be void for uncertainty, or because the beneficiary is not ascertainable or has ceased to exist or be an unlawful perpetuity, the property shall go to the heirs at law or next of kin of the decedent as if he had died intestate. See act of July 7, 1885.

The act of June 4, 1879, directs that *every will shall be considered to have been made immediately before the death of the testator* so far as the disposition of property is concerned. This has nothing to do with the requirement that a gift to charity must be made at least one month before the testator's death. It means merely that the testator is to be regarded as uttering his will at the date of his death, for it speaks his mind not only when it is made, but up to the last instant of his life. If he says, "I give all my real estate to my niece, Sarah," the niece gets all the realty which he had at the time of his death. This may be twice the amount which he had when he made the will, or again it may be only half that amount, but the will speaks as of the date of the testator's death, unless he makes it clear that he intends differently. For instance, he may say in his will, "I give my niece Sarah all the real estate which I own at the date of making this will." The subsequent acquisition of more real estate by the testator would not enlarge the devise to Sarah in that case.

If the testator leaves property to anybody, and the gift fails by reason of the beneficiary's death during the testator's lifetime, the person who was left the residue of the estate takes the amount of the gift which has failed. In other words, the failure of the gift to the beneficiary through the latter's death swells the amount of the residue by so much. The testator has a right to direct differently if he so chooses. This matter of the death of a beneficiary named in the will before the death of the testator himself often causes confusion. It is better for a testator who has made a will to bethink himself as soon as he hears of the death of a beneficiary under the will about the law on this subject. If he waits until his own death occurs, his intentions may be defeated. The general rule is that if a beneficiary dies before a testator, his estate does not get the land or money or other property left to him. If he dies a week or a day or even a minute after the testator, the beneficiary's estate gets the full benefit of the bequest, unless the testator provides otherwise in his will. *At the instant when the testator dies the status of his estate is usually fixed*, that is, the situation existing at that time usually determines who are entitled to share in the estate, whether as creditors or beneficiaries. Sometimes a testator may provide in his will for the giving of a contingent legacy, hingeing upon some future event which will not be determined until long after the testator's death.

There are some exceptions to the rule that a gift absolutely lapses if the beneficiary dies before the testator. If the beneficiary is a child or other lineal descendant of the testator, and dies before the testator, but leaves issue surviving the testator, the gift is good in favor of the issue. The same thing is true of brothers, sisters, nephews and nieces, unless the testator leaves some lineal descendant. Suppose a testator who has no descendants gives a legacy of \$500 to his niece Jane. If Jane dies before the testator, leaving issue who survive the testator, the issue of Jane take the sum of \$500. Suppose that the testator did not mention Jane by name, but directed that each of his nieces should receive the sum of \$500. The act of July 12, 1897, would entitle Jane's

issue to receive the legacy of \$500, still assuming that the testator leaves no descendant. If, for instance, he leaves a grandson, Jane's issue would not get the benefit of the gift.

The act of May 9, 1889, provides that no disposition of property for any religious or charitable use shall fail for want of a trustee or by reason of the objects ceasing, or depending upon the discretion of a last trustee, or being given in perpetuity, or in excess of the annual value limited by law; but it shall be the duty of any court having equity jurisdiction in the proper county, to supply a trustee, and by its decree to carry into effect the intent of the donor or testator, so far as the same can be ascertained and carried into effect consistently with law or equity. The reason for passing the act of 1889 was that many charitable gifts had failed through some occurrence unforeseen by the testator. The trustee appointed might refuse to act, or die. The charitable corporation to which the property was left might have corporate capacity only to receive property up to a certain amount. In order to prevent the possibility of thwarting a testator's charitable gifts by any technicality, the act of 1889 allows the courts to repair any of these defects by diverting the money which cannot go exactly as the testator intended into channels which will enable his benevolent intentions to be substantially, if not literally, carried out. No violence is to be done to the wishes of a testator, but his desires are to be achieved in the best way possible under the circumstances.

In case it seems impossible to execute a trust in a manner which will substantially reconcile the law of Pennsylvania with the intentions of the testator, the gift must fail. The act of July 7, 1885, directs accordingly that if property is left for religious, charitable, literary, educational or scientific uses, and the same shall be void for uncertainty, or if the object of the trust has altogether ceased to exist, the property shall go to the nearest relatives of the decedent, as in the case of persons who die intestate. Wherever possible, however, the testator's intentions will be carried out. In the case of *Lewis's Estate* (1892), 1 D. R. 423, it appeared that John D. Lewis, a colored Philadelphia lawyer, had left

about \$60,000. He directed that five trustees should be appointed to form a charitable corporation under Pennsylvania laws, with its headquarters in Philadelphia. It was to be named the Lewis Protective Bureau of Civil Rights, and was to take measures to prevent discrimination against colored persons in labor organizations, hotels, business houses, schools, places of amusement and cemeteries, and also to defend their rights in other respects. The testator's daughter was an invalid, and both she and his son had been delicately reared in the expectation that their father's estate would be sufficient for their wants, and were unprepared to earn a living. Each of them was given an annuity of \$400. They and the widow asked to have the trust declared void. It was contended that this was not really a charitable trust. The Orphans' Court, however, upheld it, declaring that the act of May 9, 1889, required them to give a liberal interpretation to bequests made in a spirit of public benevolence. Lewis was the possessor of his own property, and could do what he pleased with it, subject only to the widow's exemption act, and to his wife's "thirds," as treated in Chapter LIX. A will may be preposterous, eccentric, unnatural in its provisions, but a testator is permitted to make a ridiculous disposition of his property if he is mentally capable and free from undue influence, and if he does not violate any settled rule of law.

The act of June 4, 1879, directs that a general devise of the realty of a testator shall be construed to include any real estate (to which such general description or devise may extend) that the testator may have the power to dispose of by will in any manner he may think proper. Similarly, a bequest of the personal estate of the testator shall be construed to include any personal property to which such general bequest may possibly extend, which the testator has *power to appoint* in any manner he may think proper. In this way a general gift may operate not only to dispose of the testator's own property, but also to combine the execution of any powers which may have been given to the testator to dispose of other persons' property. A typical example of

the way in which this act would work out may be stated as follows: Suppose A's grandfather has left B some property for A's life, and the property is to go after A's death to such person as A may designate in his last will. If A makes a will leaving all his real and personal property to a favorite daughter, the act of 1879 would stretch the gift so as to make it cover not only A's own estate, but also the property left by A's grandfather as to which A had a power of appointment.

Except as restricted by the exemption act of 1851 (see page 642; also *Irwin's Estate* (1897), 6 D. R. 351), a person who makes a will may cut off everyone but the testator's husband or wife without a penny. The husband's interest in his wife's realty is called his "curtesy," and the wife's interest in the husband's realty her "dower." A husband's will cannot deprive his wife of her right in case there is issue, to receive one-third of his personal estate absolutely and a life interest in one-third of his realty, or, in case there is no issue, of her right to receive half his personal estate absolutely and a life interest in half his realty. The act of April 8, 1833, provides that a devise or bequest by a husband to his wife of any portion of his estate or property shall be considered to be a substitute for her dower interest in the husband's estate, unless the husband declares otherwise in his will. The widow has her choice between taking what is given her in the will, on the one hand, and her dower, on the other hand. As respects the widower, the act of May 4, 1855, directs, "that any surviving husband may, against her will, elect to take such share and interest in her real and personal estate as she can, when surviving, elect to take against his will in his estates, or otherwise to take only her real estate as tenant by the curtesy. Provided, That nothing herein contained shall affect the right or power of the wife by virtue of any authority or appointment contained in any deed or will, to grant, bequeath (or) devise as heretofore, any property held in trust for her sole and separate use." To sum up, a widow may either take the provision made for her in her husband's will or she may claim her share as prescribed by law. On the other hand, a widower has a triple

choice; he may take the provision made for him in his wife's will, or he may take all her real estate for life as tenant by the curtesy, or he may take such interest in her real and personal estate as she can, when surviving, elect to take against his will—that is, in case there is issue, one-third of her personal estate absolutely and a life interest in one-third of her realty, or in case there is no issue, half her personal estate absolutely and a life interest in half her realty.

Sometimes a widow cannot make up her mind whether to take what her husband has given her in his will, or what she would get under the intestate laws. If she has not notified the executor or administrator within a year from her husband's death, she may be cited to appear before the Orphans' Court to make her choice. If she fails to appear, the Orphans' Court will make a decree in her absence. This decree usually gives her only what was left to her by the husband's will, and she is not free afterwards to claim her dower rights.

(B) Form of will.

Most wills begin about as follows: "I, John Smith, of the City of Philadelphia, gunmaker, being of sound and disposing mind, memory and understanding, do hereby make and publish this my last will and testament, hereby revoking all prior wills or testamentary papers by me at any time heretofore made, and declaring this only to be my last will and testament." It is wise to insert a clause like that just given, declaring that prior wills and testamentary papers are revoked, for this may prevent disputes. Sometimes a letter, signed at the end, is brought forward as a testamentary paper by one to whom the decedent has promised in the letter to leave something after his death. Such a letter, or other properly signed paper which appears to be meant as a will, may be proved before the Register in the same manner as a more formal document. Promises of this kind may be revoked by the testator, unless they were based upon consideration or made under seal.

After the preliminary clause which has been explained, the first paragraph of a will usually states that the decedent's just debts and funeral expenses are to be paid as soon as convenient after his death. This clause is of no particular importance. Then the testator directs the payment of legacies to any relatives, friends or charities whom he may desire to benefit. In another clause he may choose to devise his home to his wife or some other beneficiary. In still another clause, perhaps, he may make provision for the erection of a tombstone, or arrange for the fulfilment of any other special object which he may have in view. After these matters have been provided for, it is well to make a gift of the rest, residue and remainder which may be left over after the payment of everything that has been previously mentioned. Finally, the testator usually appoints one or more executors. It is often wise to direct that the executors and trustees, if trustees are appointed, shall give corporate security, in case the testator desires to make quite certain that they will not ruin the estate through negligence or fraud. A will usually ends about as follows: "In witness whereof I have hereunto set my hand and seal this 30th day of August, 1906." The testator signs at the end, and the seal is attached to the right of the signature. The seal is not at all necessary, but if it is used a scroll or other representation of a seal may be made before the testator signs his name, and will be just as good as a wafer or wax seal.

A form of witness clause has already been given. It is not necessary that the witnesses should be made acquainted with the contents of the will, although it may be of use to inform them what is in the will, and to let them read it if there is fear that it may be contested. Under such circumstances, if the testator reads the will over to the witnesses and those who are especially benefited by the will are absent from the room at the time, this will help to repel the suspicion that the will was procured by fraud or undue influence. In the case of a blind person, it is always desirable that the entire will should be read over to him when he puts his mark or signs his name to it, and the same thing holds true of an illiterate person.

The act of 1832 enables the Register of Wills to proceed against a party who refuses to file a will which is in his custody after the decedent's death. Any person interested in having the will proved may get the Register to issue a citation, requiring the custodian of the will to produce and deposit it in the Register's office. If the person against whom the citation has been issued does not either deny having possession or control of the will within fifteen days, or produce it before the Register, he is liable to an indictment as for a misdemeanor, or to an action for damages by the person aggrieved. The Register has power also to compel the attendance of persons whose testimony may be needed in proving the will, and he can arrange for the taking of testimony not only in this state but also in other states and foreign countries. The act of 1832 has the following to say about the probate of nuncupative wills: No such will shall be admitted to probate until fourteen days after the decedent's death, or unless notice has been given to the widow, if any, and to such of his near relatives as would be entitled to administer the estate in case of intestacy. This notice is to be given, in order to enable them to contest the nuncupative will, if they so desire. No testimony can be received to prove any such will after six months have elapsed from the speaking of the alleged testamentary words, unless the said words, or the substance thereof, were put in writing within six days after the making of the nuncupative will.

(C) Will contests.

Any person interested may deny that the will was really signed by the testator, or if he does not allege that it was forged, may declare that it was executed under the pressure of fraud or undue influence, or else that the testator was not in his sound mind when the will was made. Thereupon the Register may arrange for a trial of the matter. Notice is given to those who are interested under the will, and also to those who are interested in having it set aside. A time is fixed for hearing testimony on both sides, and meetings are held before the Register, who decides whether the will shall

stand or fall. So far as the questions of law which the Register may pass upon are concerned, an appeal lies to the Orphans' Court, and from their decision to the Superior or the Supreme Court. It is different with matters of fact as to which the Register may render a decision. He is regarded as the arbiter of disputed matters of fact, and in most cases the Orphans' Court will be satisfied with his findings of fact. If dissatisfied, however, or if the questions raised present grave doubts as to the justice of the Register's decision, the Orphans' Court may send the case to the Court of Common Pleas for a trial, in order that a jury of twelve men may pass upon the disputed matters of fact.

In the matter of contesting wills, as in all legal matters, promptness and vigilance are to be recommended. Sometimes, however, a contestant does not come forward for a long time. If personal property is distributed to a beneficiary under the will, and the will is afterwards set aside, the executor who has made distribution by order of court will be protected. The only remedy of the persons who have had the will set aside will be to try to follow the proceeds of the estate into the beneficiaries' hands. The act of June 25, 1895, directs that the probate by the Register of the proper county of any will devising real estate shall be conclusive as to such realty, unless proceedings to set aside the will are started within three years from the date of probate.

(D) Revocation of wills.

The act of April 8, 1833, directs that a written will may be revoked in none but one of the following ways: first, by some later written will or codicil, or other writing, revoking the previous will, executed and proved in the same manner as a will; second, by burning, cancelling, obliterating or destroying the same by the testator himself, or by someone in his presence and by his express direction; third, by a nuncupative will which is committed to writing in the testator's lifetime, and after the writing thereof read to or by him, and allowed by him, and proved to be so done by two or more

witnesses. This third method of revoking a written will by a nuncupative will cannot affect any provisions in the written will concerning real estate. The repeal of provisions in a written will concerning real estate must be effected by one of the first two methods of revocation.

The act of 1833 also provides that when any person makes a will, and afterwards marries or has a child or children not provided for in his will, and dies leaving a widow or child, although the child be posthumous, every such testator shall, so far as regards the widow or child be deemed to die intestate, and such widow, child or children shall be entitled to such shares of the estate of the decedent, as if he had actually died intestate. Under this act, if the child is born after the making of the will, but has been provided for in it, the will is not affected. Again, if the will has been made just before the marriage, and the testator has provided for his fiancée, who afterwards became his wife, the will is not disturbed, unless the widow so desires. It is often wise for a married man when he is making a will to provide not only for his living children, if any, but also for those who may be subsequently born to him.

This act does not affect the will of a man, so far as his family are concerned, unless they really survive him. If he makes a will, say, in 1900, marries in 1901, and his wife dies in 1902, his old will is still good, should he die in 1904, except so far as the children of the marriage may be concerned. If a single woman makes a will in 1900, marries in 1901, and her husband dies in 1902, the will is not revived by her husband's death, and upon her death in 1904, without making any other will, she is to be considered intestate. These provisions for the revocation of a will by marriage or birth of children do not apply to the disposition of personal estate by a testator whose domicile is outside of the Commonwealth of Pennsylvania.

CHAPTER LXI.

TRUST ESTATES.

A trust is defined as a right of property held by one party for the benefit of another. The property may be real or personal. The party who holds the property is called the trustee, while the beneficiary is called the *cestui que trust*. Where one person holds property which belongs to another, the owner is usually entitled to demand that his property be delivered to him. If it is real estate, and has been leased to a tenant, the latter has the right of possession during the term of the lease. The owner, however, continues to hold the title, and may sell it at any time, subject to the tenant's rights. Again, the owner of personal property who has pledged it for a loan, retains ownership. The pledgee has possession, together with a lien upon it to secure repayment of the loan, but the owner may sell it subject to the pledgee's rights.

In the case of a trust, the beneficiary who enjoys the income from the trust estate is not, strictly speaking, the owner of it. The law recognizes a number of situations in which it is proper to make a provision for the benefit of certain persons, but to keep the actual legal ownership and control of the property out of them. This is often done by appointing a trustee, who holds the legal title, while the equitable title is lodged in the *cestui que trust*, the beneficiary. The trust may be formed during the lifetime of the creator, who signs and delivers a deed of trust, or otherwise puts property in trust for beneficiaries. Another way of creating such express trusts is by will. What is to be said on the subject applies to both kinds of trusts.

(A) Various kinds of trusts.

If a man signs a deed conveying a certain house and lot to John Smith in trust for Edward Jones, and no special reason appears in the deed of trust for creating a trust, the deed is not good as a trust deed, and an absolute title passes

to Jones. He is entitled to take charge of the property, and to dispose of it as he pleases, and Smith can have nothing to say about the matter. Jones is the beneficiary, and the courts can see no good reason for Smith's interfering with the property. This is called a dry trust, and it exists where a trustee is given the legal title, but no object is to be gained by depriving the beneficiary of any of the incidents of ownership. If the deed of trust for Jones had been couched in the terms of a *spendthrift trust*, so that the intention of the creator of the trust would seem to be to prevent Jones from squandering the estate, then the law would uphold the trust, and Smith would be a real trustee. What is the practical difference between the two cases? Where the trust is a dry trust, and no reason appears for it, Jones, the beneficiary, may sell the property, and do with it what he pleases. The law presumes that he can manage it as well as Smith, and since he was made the owner of it, he should be given the right to control it. In the second case the provisions of the trust indicate that the creator of it feared that Jones might lose the benefit of the estate by wasteful expenditures. The terms of a spendthrift trust usually provide that the property shall be held by the trustee without liability to execution or attachment in any suit or for any judgment against the beneficiary. When judges find clauses of this kind in a trust deed, they understand that there was a substantial reason for putting the legal title in a trustee, and giving merely the income to the beneficiary. The courts allow beneficiaries to be protected against the consequences of their own prodigality. Accordingly, in a spendthrift trust, even if the beneficiary should want to sign away his rights to a stranger, any agreement which he may make will not be enforceable. The trust estate still remains intact, and the income is paid directly to the beneficiary himself.

This is one kind of trust in which the courts see the advisability of keeping the legal title separate from the equitable title. If a spendthrift trust is to be created, the specific intention to do so should appear plainly. The words which are often used to denote the intention to create a spendthrift

trust are as follows: "Provided that the trust estate hereby created shall not be subject to any attachment or execution against any of the beneficiaries, nor to any assignment or contract which the beneficiaries may make, by anticipation or otherwise. Payments to be made directly to the beneficiaries."

Another reason for the creation of trusts is to preserve the trust funds, and keep the trust estate intact for the protection of those who have not a present interest in the estate, but may have it at some future time. Where the rights of absent beneficiaries are concerned, and especially where these beneficiaries are not yet in being, the courts are anxious to prevent the dissipation of the trust funds. It sometimes happens that the beneficiaries provided for never come into existence. A provision may be made for unborn children, and the children may never as a matter of fact be born, but as long as there is a possibility that they will be born, the courts are on the alert to preserve their rights.

If property is left to Q, but Q's rights are subject to be divested upon the birth of any children to X, the law considers that X may possibly have children, even though he is ninety years old, and the trust will be kept alive until the legal possibility of X's having children has vanished. If X dies leaving a wife, then the trust may be kept alive for a further period of, perhaps, nine months. If X dies without leaving a wife, the trust ceases to exist upon his death. If the trust is in favor of Q, but is subject to be divested if any children are born to X by his wife C, then, of course, the trust falls whenever C dies without having children born to X, or, say nine months after X's death without children born to him by C. All this shows that where there is a trust for future beneficiaries, who may or may not come into being, the law steadfastly upholds the trust while any possibility that there will be beneficiaries still remains.

The case of *Bayard's Estate* (1897), 6 D. R. 206, illustrates this doctrine. The testator left one-fifth of his residuary estate to his son, Richard, directing that the same should be invested, and the income paid to Richard's widow Ellen during her life. At the time of her death the executors

were to turn over the principal of the said fifth part to the child or children of Richard, and the lawful issue of such as might be dead. The widow and the only two children of Richard petitioned to have the trust vacated. It did not appear that the trust was a spendthrift trust, so that there was no reason to protect the parties against the consequences of their own extravagance. The trust would not come under the description of a married woman's trust, which we will take up hereafter. Accordingly, the argument of the widow and two children was that they were the only persons interested, and that they should be allowed to enjoy the principal of the trust estate. The Orphans' Court pointed out, however, that the final ascertainment of the children's rights was not to take place until after the widow's death. Richard's children had vested rights in the remainder of the estate, to be enjoyed after their mother's death, but these rights were subject to being divested by the death of either child before his mother. The period for the absolute ascertainment of the rights was postponed until the moment of the mother's death, so that the court could not be sure but that one or both of the children would die before the mother, leaving issue, for whom in that contingency the will provided. The children, therefore, could not declare that they were the only issue interested, since when the time of distribution should arrive they might be dead for all the court could tell. The petition was, therefore, dismissed. Everyone may usually relinquish a provision intended for his own benefit, and this maxim enables many trusts to be set aside upon the request of all the parties for whose protection it was created. If the trust is a spendthrift trust or a married woman's trust, or if some of the beneficiaries are minors, a different rule would apply, but where all are of full age and under no disability, and all join in the petition to vacate the trust, it may be done. This does not, however, authorize one person to renounce the benefits of the trust for any other than himself. Furthermore, said the court, those who presented the petition were not entitled to anything apart from the will. A man's widow may partially break his will, if he attempts

to leave everything in trust, because she is entitled to receive a certain share of the personalty absolutely, and a life interest in a certain portion of the realty. Ellen Bayard, however, was not the widow of the decedent, but the widow of his son Richard, so that she could not claim except through the will.

Just above mention is made of a *married woman's trust*, which is somewhat like a spendthrift trust. The married woman sometimes needs to be protected from her husband, just as the spendthrift needs to be protected from himself. If a trust is created for the sole use of a woman who is already married, or who is engaged to be married, the law will uphold the trust, and will not permit it to be vacated at the instance of the married woman herself. This kind of trust is often created by the father of a girl who is engaged or actually married to a worthless man, or to one in whose business ability the girl's father has little confidence. We saw in the case of a spendthrift trust that certain words are often employed to indicate in a formal way the intention to create such a trust. In the case of a married woman's trust also it is customary to use certain words which will help to show to the courts the specific intention to found such a trust. These words are usually "for her sole and separate use, free from the control of her husband." Other words with a similar meaning may be used, but it is better to employ the phrase which has acquired the sanction of custom.

A married woman's trust may be created either by a deed of trust during the creator's lifetime or by a will. If it appears that the woman to be benefited was neither married nor in contemplation of marriage when the deed or will was made, the trust fails, and the woman may demand that the trustee shall deliver the property over to her absolutely, and freed of all trusts. It would seem, therefore, that it is always wise to join in any married woman's trust appropriate words which will make the trust also a spendthrift trust, because the spendthrift trust does not depend on the fact of actual or contemplated marriage. It holds good whether or not there is actually any extravagance shown by

the beneficiary. A spendthrift trust may be created for unborn beneficiaries. If a married woman's trust is vacated and set aside, her creditors may swoop down upon her, and sell out the property left for her benefit; or her husband may persuade her to demand the trust funds and give them to him for investment, and her private fortune will perhaps be lost.

There is another reason for coupling spendthrift trust provisions with provisions to create a married woman's trust. Suppose a married woman's trust is made when the beneficiary is actually married, so that it takes effect properly as a married woman's trust. As soon as the husband dies, the trust terminates. Even if she becomes married a second time, the trust does not revive upon her remarriage.

Many trust estates come under the jurisdiction of the Court of Common Pleas, rather than of the Orphans' Court. The Orphans' Court has jurisdiction over all trusts created by will, whether the trustees are appointed by name, or executors are appointed, and the trust estate is not left in charge of the executors by name, but merely by reference to their position. The Common Pleas Court has jurisdiction concurrently with the Orphans' Court over testamentary trusts where the trustee is appointed by name, even though he happens to be also the executor. In case, however, a testator appoints certain executors, and in the same will creates a trust estate to take charge of which he appoints his executors, without naming them, the Court of Common Pleas has no jurisdiction. Even where the Common Pleas Court has concurrent jurisdiction over testamentary trusts, it is customary to have such trusts carried out under the supervision of the Orphans' Court. In the case of trusts created by a deed or agreement among living persons, the Court of Common Pleas usually has sole jurisdiction. The Orphans' Court, however, is frequently called upon, even in the case of such trusts, to appoint guardians for minors, where this becomes necessary. The U. S. District Court has jurisdiction over bankruptcy trustees. The state Courts of

Common Pleas have jurisdiction over assignees of insolvent estates which are being administered under state laws.

Under the act of March 30, 1905, the Orphans' Court may appoint a *trustee durante absentia*, that is a trustee in the absence of a person who leaves property which needs a regular caretaker. The husband, wife, or next of kin of the absentee, or some other person interested, may present a petition to the Orphans' Court of the county where the greater portion of his property in Pennsylvania is located, stating that the absentee has been away from his usual abode for one year, and that his whereabouts have not been known during that period, and that he has left an estate without any person to manage it. This petition is made under oath, and must be supported by the affidavit of at least one disinterested resident (and in certain cases of at least two residents) of the ward, borough or township or other territorial subdivision where the absentee resided. If a man has gone away, and left another with full power to take charge of his property during his absence, there is no reason to appoint a trustee *durante absentia*. When such a trustee is appointed, he must give bond before taking charge of the estate for twice the amount of the personal property and also twice the amount of seven years' rental of the real estate. His sureties must be approved by the court, and he must file an inventory within thirty days after his appointment, and render an account at least once in three years, or oftener, if required by the court. This provision for periodical accounting is similar to that in the case of a guardian, who should file a partial account at least once every three years, and a final account after his ward comes of age. The general rule for accounting in the Orphans' Court is that those who are under its jurisdiction should render an account at least once every three years. There is not the same necessity for periodical accounting in the case of trustees who are under the supervision of the Common Pleas Court. In concluding our brief survey of trusteeships *durante absentia*, we should note that the estate of the absentee may be distributed under the direction of the Orphans' Court after seven years

from the trustee's appointment, or sooner, if the death of the absentee shall be established by satisfactory evidence. Upon the absentee's return before distribution, the trustee must render an account, and restore the estate after deducting the reasonable expenses of managing it, and compensation for the trustee. The act of June 24, 1885, provides for granting letters of administration upon the estate of one who has been absent for seven years, and the act of April 14, 1905, makes a certain provision for the probating of an absentee's will.

(B) Rights, powers and duties of trustees.

When any executor, administrator, guardian or trustee has moneys in his possession of which he is to distribute the income, and which are to remain for a long time, he may invest them in United States or State of Pennsylvania bonds or the bonds of any Pennsylvania county, city, school district or other municipal corporation, or in first mortgages. An executor or administrator should not invest, as a rule, without getting the sanction of the Orphans' Court, for he is expected to close up the estate and to convert it as far as convenient into cash. It is the trustee's duty to try to make the estate produce an income. Hence, he may be surcharged with interest which should have been derived from the estate, if he has permitted large sums to remain uninvested for a long time. A trustee may usually invest funds in any of the above named securities without asking leave of court. He may, under the act of April 13, 1854, invest in ground-rents with the court's permission. Many trustees are given wide discretion to go outside of the limits of what are strictly legal investments, in order that the trust estate may obtain a bigger income. Even where a large range of discretion is given to a trustee by the terms of a trust, he should not throw caution to the winds, and invest indiscriminately. A great deal will depend upon the particular terms of the trust, but certain general rules may be laid down. A trustee empowered to invest trust moneys in any property, real or personal, that he may see fit, must invest judiciously, and should

not only carefully secure the principal, but obtain an immediate income. Even though the creator of the trust declares that he commits everything to the judgment of the trustee, the trustee will not be relieved from liability for gross negligence. In one case it appeared that a trustee had been given discretion to invest in stocks, bonds, mortgages or other securities, real or personal. He put a lot of money in a limited partnership, and the court held that this was not an investment in securities, but in the hazard of trade. If an investment is made in bonds, it is usually wiser to invest in registered, rather than in coupon bonds. The principal of coupon bonds is seldom registered, and, being usually negotiable, they often pass by delivery. The trustee should have all the securities taken and registered in the name of the estate, or in his name as trustee for the estate, rather than in his name alone. Likewise, the trust moneys should be deposited in a separate account to the credit of the estate.

The management of a trust estate may continue for years, and carelessness in any degree may cause heavy loss in the long run. The trustee should take receipts for any payments to beneficiaries. He should not usually permit them to anticipate their income. This sometimes leads to trouble where a life tenant to whom income is advanced ahead of time suddenly dies. The life tenant's income stops short upon his death, and the trustee may be unable to recoup himself, for the remainder-man cannot be charged for money advanced to the life tenant.

The *compensation* of a trustee is usually five per cent on the income, as derived from time to time, and also five per cent on the principal when that is finally distributed. This rule is subject to the same modifications as in the case of an executor's compensation. Under special circumstances, the court may allow compensation based on the size of the principal of the trust estate before the time for final distribution and discharge of the trustee arrives. Usually, however, the trustee must content himself until that time comes with only commissions on the income. He must not pay the gross income to the life tenant, and then on the

life tenant's death try to hold subsequent income due the remainder-man for payment of commissions already earned. The commissions should be deducted when payments to the life tenant are made from time to time.

Much of what is said in Chapter LVIII about executors' and administrators' accounts is applicable to those of trustees. The act of June 3, 1903, requires all executors, trustees and other fiduciaries to give their sureties, upon request, a detailed statement showing how the trust funds are invested.

A trustee should be constantly ready with his accounts, and he should be prepared to show by legal evidence that they are just and true. All doubts and obscurities in an account filed by him are to be taken adversely to him. In the case of *Mintz v. Brock* (1899), 193 Pa. 294, a trustee's account extended over several years, and he claimed a credit of \$110 for postage stamps, stationery, telegrams and incidental items. He also claimed a credit of \$1,451 for certain items of discount and exchange on checks sent from Marionville, Forest County, to Buffalo. No statement was produced showing on what notes discount was paid, or when he had paid it. The court disallowed all the items of credit just mentioned. The trustee's duty was to keep itemized books showing all moneys paid out, and he could not gain credit by swearing to lumping charges. In the same case it appeared that the trustee, who was conducting a lumber business for the beneficiaries, had filed an account only when forced to do so by a suit in equity. He claimed credit for counsel fees in the preparation and defense of the suit, which was decided against him. This credit was disallowed, since he was virtually seeking to be reimbursed for his expenses in endeavoring to defeat the trust.

It is the duty of a trustee to exhibit his books and accounts at all reasonable times to those who have the right to inspect them, including sureties and remainder-men whose interests have not yet arisen. The courts will protect him from unnecessary and vexatious interference. Where there are a number of beneficiaries, each of whom is entitled to income, the trustees should not favor one at another's ex-

pense, and his account should show how each one stands as respects distribution of income or principal. He should also keep matters of distribution apart from matters of administration, and he should keep principal account apart from income account, and personalty apart from realty account.

A trustee will be required to file an account in court when any good reason for so doing appears, and particularly when the trust estate is to be finally wound up. No lapse of time, even for more than twenty years, conclusively bars the beneficiaries' right to an accounting and to the payment of the balance found due. The courts are disposed, however, to dismiss a petition to compel an accounting if the beneficiaries have delayed for over twenty years in asserting their rights, and no good explanation for the delay can be given. Where there has been a private settlement between trustee and beneficiaries, this will take the place of a formal accounting before the court, but a private adjustment may be set aside if there is any suspicion of unfairness.

(C) Limits upon the duration of trust estates and upon the accumulation of income.

In the case of a trust for a public charity, there is no reason why the trust estate should not be kept intact permanently, and only the income used for the charity. A different situation presents itself when a testator wants to keep his property in his own family for many future generations. No such public good is to be accomplished as in the case of a general charity. The testator cannot anticipate conditions as well as he can if he is founding a public charity. There is no occasion for the courts to put their expensive machinery at the service of a man desirous of providing for very distant descendants, whose rights cannot become enforceable until after many years, and for whom the testator is under no obligation to provide. He cannot be supposed to cherish a real affection for distant descendants, and no tie of blood is disregarded by denying him the power of making a valid trust in their favor. On the contrary, the policy of our American law is to have estates distributed.

Feudal conditions introduced the law of primogeniture into England, and family pride, together with a number of other reasons, still maintain it there. In the United States the idea is that the eldest son is ordinarily no better entitled to his father's estate than any of his brothers and sisters. Likewise the English law which prefers males over females has no place here.

How far, therefore, will the law of Pennsylvania permit a trust estate to be tied up? The exact number of years during which it may be preserved is not laid down. The only rule that we can go by is the one called "the rule against perpetuities." This rule directs that no interest, subject to a condition precedent, is good unless the condition must be fulfilled, if at all, within the period of some life or lives in being at the creation of the interest and twenty-one years thereafter. In other words, the interest must vest within twenty-one years after the expiration of some life which was in being at the time the interest was originally created. Suppose the testator provides that his property shall be held in trust for twenty-two years, and then distributed among those who shall be found to be his living descendants at the expiration of this period. This is not a good provision, because it violates the rule. A testator may direct that his estate shall be held on certain trusts during the life of the grandchild (among all the grandchildren that are living at the time of the testator's death) who shall survive the testator the longest, and that twenty-one years after the death of said grandchild, the property shall vest in all those who at the time of the death of the said survivor are found to be the testator's descendants. In this second case the rule is complied with, although probably the estate will be tied up for many more years than twenty-two. If the testator provides that the estate shall be vested in those who are found to be his descendants upon the death of that particular grandchild, who shall be the survivor of all the testator's grandchildren, the provision is in conflict with the rule against perpetuities. It may well be that grandchildren will be born long after the testator's death. The difference

between this last provision and the one mentioned before is that in the former case the grandchild whose life was to help measure the duration of the trust was by the terms of the will to be one of the grandchildren actually living at the testator's death.

The rule against perpetuities requires that a future interest, in order to be valid, must be such as will surely *vest*, if at all, within a certain period. An interest is vested when the identity of the beneficiary is certainly determined, and there is a present fixed right of future enjoyment. If a man leaves property for such of his great-grandchildren as shall survive his last grandchild, the absolute right of any great-grandchild to participate in the fund will not be ascertainable until the time of the death of the last surviving grandchild. Until that time arrives, the number of favored great-grandchildren is subject to increase or decrease. As we saw before, this future date is postponed too long, if the testator delays it until the death of his last grandchild, for very likely the last survivor of his grandchildren may happen to be one born after the testator dies. What the testator may do is to direct that his property must be kept intact, except for the distribution of income during the life of that particular grandchild, *alive at the time of the testator's death*, who survives all the other grandchildren that were alive at the testator's death, and that his property shall be continued intact for twenty-one years after the death of this particular grandchild, and then distributed among such of the great-grandchildren of the testator as may be living at the expiration of the said twenty-one years.

The rule against perpetuities forbids the creation of a trust which is to last beyond the term allowed, when made by a deed during the donor's lifetime, just as much as if he were to make it by a will, to take effect upon his death.

The act of April 18, 1853, restrains the accumulation of income. It directs that no person shall dispose of realty or personalty, either by deed of trust during the owner's lifetime or by will, so that the income thereof shall be wholly or partially accumulated for any longer period than the life or

lives of the creators of the fund and twenty-one years thereafter. Furthermore, this period of twenty-one years must be on account of the minority of the beneficiaries. In the rule against perpetuities the period of twenty-one years has no necessary reference to the minority of the beneficiaries, but under the accumulations act, the income is allowed to accumulate only during the actual minority of the beneficiaries. The act of 1853 excepted from its operation any donation for literary, scientific, charitable or religious purposes. The act of April 26, 1855, however, provided that the property so accumulated must never be allowed to exceed the limit imposed by law upon the property of the corporation, or the limit of the annual income thereof. The maximum yearly income which such corporations may derive is fixed at \$30,000 by the act of April 22, 1889.

The statute against accumulations is in many respects like the rule against perpetuities, but there is this difference between them: If the rule against perpetuities is violated, all or a large part of the trust provisions may become absolutely void. See, however, *Clapier's Estate* (1906), 15 D. R. 540. If the statute against accumulations is violated, the accumulation may continue for twenty-one years, but not beyond. Even a partial accumulation of income is forbidden except within the bounds set by the act. It has been held, however, that if a spendthrift trust is created for the benefit of a son, to last during his entire life, and the trustee is to give the son only such part of the income as he thinks necessary, the trustee may invest the balance for the son's benefit. This partial accumulation is not intended to be permanent, but only temporary and in the interest of judicious management. The court may allow the trustee to invest the balance of income not needed for the son, even though he has reached full age.

INDEX.

[See also Table of Contents.]

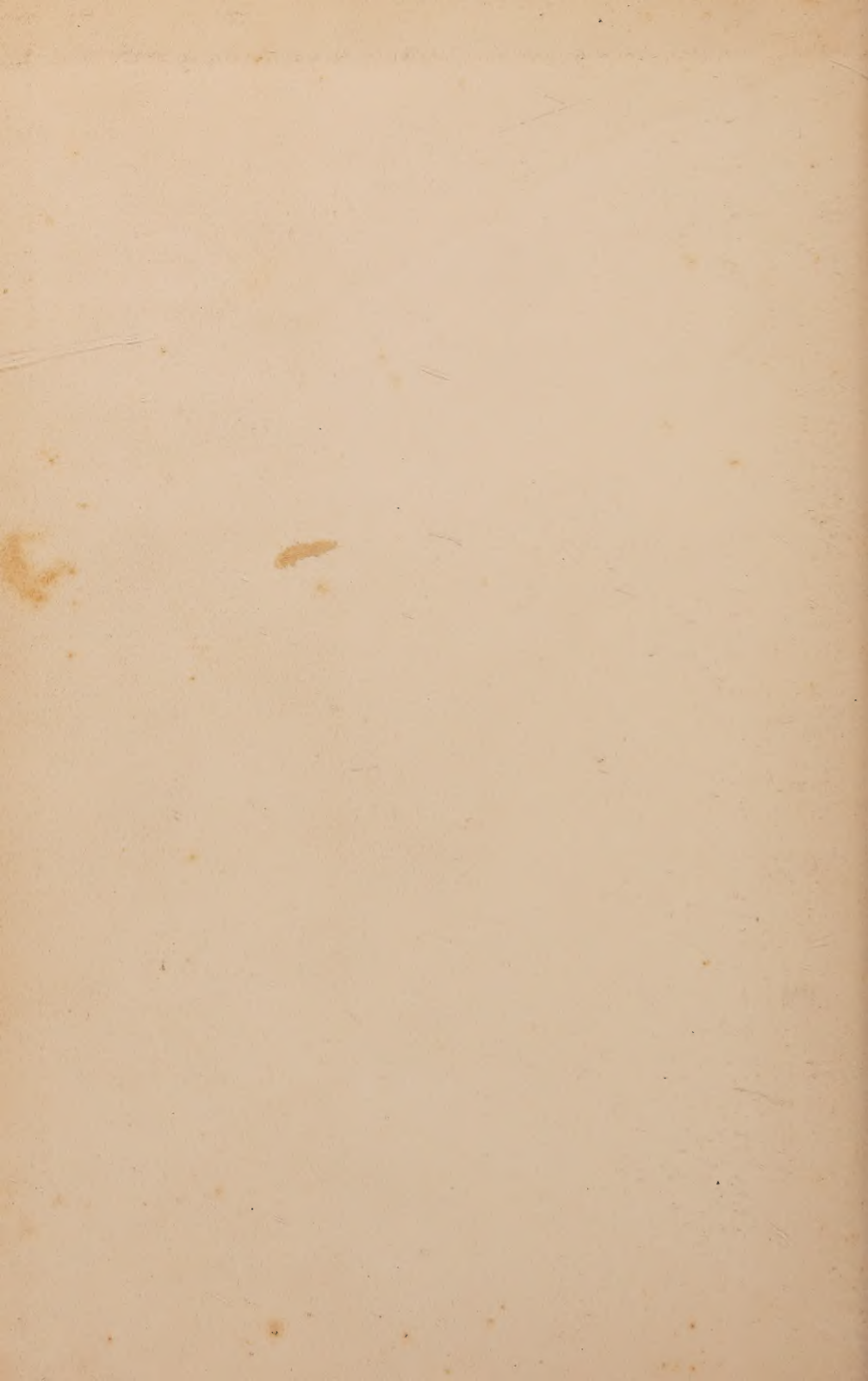
- Accommodation party, 97, 98, 140, 150-151.
- Accountant, employment of, by executor, 648.
- Accounting,
 - of corporations, 422-423.
 - by assignees, 264-267.
 - by executors, 644-659, 692, 695.
 - by guardian, 692.
 - by partner, 302, 320-324.
 - false corporate, 419.
 - in real estate settlement, 542, 544, 546.
 - by trustees in the state courts, 692, 695, 696.
 - by trustees of a bankrupt estate, 242-245.
 - necessity for periodical, 692.
- See FORMS OF ACCOUNTS.
- Administrator, 137, 333, 609-662.
- Advertisements, 34.
 - by executors, 622.
 - of application for charter, 353, 356.
- Affirmance of voidable contracts, 107.
- Agency, 41, 273-291, 311-318.
- Alteration of contract, 55, 166.
 - of suretyship or guaranty contract, 568-570.
- Ancillary, 612.
- Apprenticeship, 131-132.
- Auction sales, 46-47.
- Baggage, 453, 472-475.
- Bailment, 77, 439-475.
- Bankruptcy, 71, 80, 137, 281, 308-309, 364-372.
 - Federal Act, 198-242.
- See INSOLVENCY.
- Bids, 33, 46-47.
- Bill of exchange, 142.
- Bill of lading, 180, 466-467.
- Bonus, 347-348.
- Boycott, 122.
- Bucket shop transactions, 117.
- Builders, 456.
- Building associations, 118.
- Capacity to contract, 84-101.
- Caveat emptor, 502.
- Certificate of incorporation, 350.
- Certificate of stock, 375.
- Cestui que trust, 126.
- Charity, gift in will to, 676.
- Charter of a corporation, 350.
- Chattel mortgage, 459-462.
- Checks, 143, 177.
- Collateral security, 378-380, 446.
- Commissions,
 - of executors, 649-652.
 - of trustees, 694-695.
- Common carriers, 452, 462-475.
- Composition with creditors, 70-71, 80, 208-209.
- Compound interest, 384.
- Compromise of actions, 67-69, 113-114, 119.
- Conditional sales, 480-484.
- Consideration,
 - adequacy of, 63-66, 68-72.
 - definition of, 60-62.
 - moral obligation, 78, 80-81.
- Constitution, 115.
- Contract,
 - assignment of, 134-137.
 - breach of, 189-195.
 - capacity of parties, 84-101.
 - communication of acceptance, 40-45, 47-48.
 - communication of offer, 39-40.
 - consideration, 59-84.
 - death of offeror, 51.
 - definiteness necessary to, 25-30.
 - definition of, 19.
 - discharge of, 74-76, 185-272.
 - executory, 66-67.
 - formality necessary to, 28, 123-133.
 - intention to enter, 20, 30-34.
 - interpretation of, 181-184.
 - lapse of an offer, 49-51, 53.
 - legality of object, 114-122.
 - necessary elements of, 19.
 - offer and acceptance, 23-56.
 - operation of, 133-180.
 - reality of consent, 101-114.
 - seal, 57-59.
 - to sell realty, 534-540.
 - when made, 54.
 - when to be implied, 34-39, 43, 51-53, 449, 647-648.
 - withdrawal of an offer, 45-49.
- Corporations, 73-74, 85, 99-101, 123, 299, 349-437.
 - accounts, 422-423.
 - application for charter, 353-357.
 - assessments, 407-410.
 - bonds, 383.
 - by-laws, 357-358.
 - certificate of incorporation, 357.
 - certificate of stock, 375, 382-383.
 - compound interest, 384.
 - corporate stock, 376.
 - coupons, 384.
 - cumulative dividends, 388.
 - cumulative voting, 393-394, 397.
 - directors, 374, 396-397, 411-420.
 - dividends, 385-390.
 - foreign corporations, 99-101, 420-437.
 - foreigner, director or stockholder, 374.
 - holding of real estate, 429.
 - increase of capital, 397, 398-399.
 - issue of stock, 359, 380-382.

[See also Table of Contents.]

- Corporations,
 lease of corporate property, 428-429.
 pledge of stock, 379, 388, 446.
 power of attorney to transfer stock, 377-378, 382.
 power of, to buy corporate stock, 376.
 powers of president, 382, 420-421.
 promoters, 73-74, 359-360.
 proxy, 392, 394.
 quorum, 395, 413.
 receivers, 363, 365-371.
 reduction of capital, 397.
 renewal of charter, 362.
 stock dividend, 388.
 stolen bonds, 384.
 subscription to stock, 390, 402-406.
 voting trusts, 374-375.
 woman organizer or director, 397.
- Coupons, 384.
- Creditors, 112, 318-320, 332, 563, 626.
- Crime, 95, 99, 113-114, 119, 284, 289.
- Cumulative dividends, 388.
- Cumulative voting, 393-394, 397.
- Curtsey, 98, 663, 680.
- Damages, 125, 190-191, 194, 299.
- Days of grace, 160.
- Debts of decedent, priority, 634.
- Deed, 535, 553-555.
 recording of, 546-548.
- Discrimination, 468-470.
- Distrain, 522-524.
- Dormant partner, 325.
- Dower, 538, 663, 680.
- Drafts, 142.
- Drunkenness, 95-97.
- Duress, 113.
- Ejectment, 525-526.
- Escheat, 671.
- Escrow, 541.
- Estoppel, 93, 275-276, 300-301, 303, 421, 489-490, 532-533.
- Evidence, relating to contracts, 181-183.
- Executed contracts, 477.
- Executor, 91, 137, 333, 609-662.
- Executory contract, 66-67, 477.
- Exemptions, 196, 522-524, 642-643.
- Factor's Act, 453-455.
See BAILMENTS.
- Fellow servant, 285.
- Fixtures, 530-532.
- Force, 112-114.
- Foreign corporations, 99-101, 429-437.
- Foreigners, 100-101.
- Forms,
 accounts in bankruptcy, 242-246.
 accounts in real estate settlement, 542, 544, 546.
 acknowledgment, 514.
 administrator's account, 653-655.
 agreement to sell realty, 536-537.
 bill of exchange, 142.
 chattel mortgage, 460-461.
 contract of suretyship, 517, 580-581.
 contract under seal, 59.
 deed, 553-555.
 draft, 142.
- Forms,
 fire policy, 596-600.
 instalment leases, 483-484, 485.
 lease, 514-516.
 mortgage clause, 601-602.
 notice of dissolution of partnership, 304.
 order to satisfy award, 660.
 partnership articles, 296-298.
 pledge of stock, 379.
 power of attorney to transfer stock, 377.
 promissory note, 140.
 quit-claim deed, 551.
 will, clauses in, 675, 681, 682.
- Fraud, 104, 106-110, 112, 380-382, 503-504, 565-566.
- Gambling contracts, 116, 117, 179.
- Gifts, 111, 641, 676.
- Good will, 83, 121, 308, 629.
- Grace, days of, 160.
- Grantor and grantee, 541.
- Ground-rents, 556-557, 693.
- Guaranty—*See* SURETYSHIP AND GUARANTY.
- Guardian, 88, 91, 692.
- Holder in due course, 141, 150, 154, 155.
- Holiday, 116.
- Implied, 508, 527.
- Infants—*See* MINORS.
- Innkeepers, 453.
- Insanity, 95-97.
- Insolvency,
 Pennsylvania Acts concerning, 246-272, 308-309, 333, 364-372.
See BANKRUPTCY.
- Instalment leases, 480-485.
- Insurance, 85, 582-607.
- Intention, in contracts, 183-184, 192, 193.
- Interest, 117, 324, 635-636, 641, 651.
- Joint-stock associations, 335.
- Labor Unions, 122.
- Legal investments, 630, 693-694.
- Licenses, 86.
- Liens, 449-455, 498-499, 545, 556, 626, 635.
- Limited partnership associations, 334-348.
- Liquidated damages, 190-191, 539-540.
- Lost property, 451.
- Mail, notice of dishonor by, 162, 163.
- Marriage, 90, 96, 122.
- Married women,
 consent to husband's deed, 538.
 contractual powers, 97-98.
 crimes of, 99.
 suits by and against, 98-99.
 trusts for, 690.
- Master and servant, 90.
 apprenticeship, 131-132, 286.
 protection of servant, 285-287.
- Minors,
 apprenticeship, 131-132.
 capacity for crime, 95.
 contractual powers, 87-95.

[See also *Table of Contents.*]

- Minors,
 - crimes of, 95.
 - employment of, 90, 132, 286.
- Misrepresentation, 104-106.
- Mistake, 102-104.
- Monopoly, 120.
- Moral obligation, 78, 81.
- Mortgage, 127-128, 549, 556-558, 584, 593, 625, 693.
- Necessaries, 87-90, 96.
- Negligence, 285-286, 289.
- Negotiable instruments,
 - bills of lading negotiable, 180, 447, 467.
 - for gambling debts, 117.
 - Pennsylvania acts concerning, 144-180.
- Next of kin, 668-671.
- Novation, 74-76, 186.
- Nuncupative wills, 674-675, 683.
- Obligor, 575.
- Option contracts, 46.
- Outlawry of debts, 78, 79.
- Partner's interest, 310, 311.
- Partnerships, 292-348.
- Past consideration, 412.
- Personal property, 97, 439-509.
- Pledge, 379, 388, 446, 459.
- Power,
 - coupled with interest, 280, 375.
 - of attorney, 377.
 - of appointment, 679-680.
- Promoters, 73-74, 359-360.
- Quitclaim deed, 551, 553.
- Quotation of prices, 31-33.
- Real property, 97, 100, 123-127, 136-137, 346, 511-559.
- Receiver, 363, 368-371.
- Recording, 327-329, 336, 343, 354, 546-549.
- Refunding bond, 633.
- Registered partnerships, 341.
- Release, 79, 124, 185-186.
- Rent, 510-512, 521-522.
- Repairs under a lease, 528-530.
- Restraint of trade, 82-83, 120-121.
- Reward, offer of, 39-40, 50-51.
- Sample, sale by, 508.
- Seal, 57-59, 60, 82-83, 132.
- Set-off, 110, 139, 188, 445.
- Severable contracts, 193.
- Short certificate, 627.
- Special partnership, 325-334.
- Spendthrift trusts, 687-688.
- Statutes,
 - of frauds, 123-125, 273, 274, 512, 534, 561.
 - of limitations, 78, 79, 93, 194, 407, 446.
- Stoppage in transit, 499-501.
- Sub-agent, 281, 283, 288.
- Sub-letting by tenant, 517, 523, 526, 527.
- Subrogation, 578, 593, 595.
- Subscriptions,
 - to charity, 65-66, 72-73.
 - to corporations, 73-74, 123, 335, 390, 402-406.
- Substituted contract, 74-76, 186.
- Suicide, 607.
- Sunday, 115-116, 178.
- Suretyship and guaranty, 129-131, 559-581.
- Tender of performance, 187-188.
- Title insurance, 537, 538-539.
- Torts, 94-95, 284, 289, 318.
- Trademarks, 476.
- Trusts, 104, 111-112, 122, 125-127, 133-134, 137, 223, 389, 686-699.
- Undisclosed principal, 284, 290, 291.
- Undue influence, 110-112.
- Usury, 117-118.
- Vendor and vendee, 477.
- Voidable contracts, 87, 91-93, 97, 107, 112.
- Voting trust, 374-375.
- Wages,
 - assignment of, 136.
 - due from corporations, 411.
 - priority of, 196-197.
- Warehouseman, 180, 465.
- Warranty, 108-109, 192, 504-509, 555-556, 589.
- Way-going crop, 532.
- Wills, 90, 111, 673-685.
- Witnesses, 675-676.
- Writing,
 - required in realty contracts, 123-125.
 - required in trusts as to realty, 125-127.
 - required in mortgages, 127-128.
 - required in suretyship and guaranty, 129-131, 561.
 - required in apprenticeship contracts, 131-132.
- advantages of, 181-183, 636-637.



F. M. SNYDER.

